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SBA'S OPINION MOLDER POLICY, AND H.R. 1157

HEARINGS

BEFORE THE

**SUBCOMMITTEE ON EXPORT OPPORTUNITIES
AND SPECIAL SMALL BUSINESS PROBLEMS**

OF THE

**COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES**

NINETY-EIGHTH CONGRESS

FIRST AND SECOND SESSIONS

WASHINGTON, D.C., NOVEMBER 15, 1983 AND MARCH 7, 1984

Printed for the use of the Committee on Small Business



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON : 1984

29-458 O

H721-26

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SBA'S OPINION MOLDER POLICY, AND H.R. 1157

TUESDAY, NOVEMBER 15, 1983

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON EXPORT OPPORTUNITIES AND
SPECIAL SMALL BUSINESS PROBLEMS,
COMMITTEE ON SMALL BUSINESS,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:35 a.m., in room 2359-A, Rayburn House Office Building, Hon. Andy Ireland (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN IRELAND

Mr. IRELAND. Good morning. I would like to call our meeting together this morning and wish you all a good morning.

We are here to discuss the Small Business Administration's opinion molder policy which has caused quite a bit of controversy over the years. The opinion molder policy was established by the SBA Loan Policy Board at the inception of the agency, continuing the same policy established by its predecessor, the Reconstruction Finance Corporation. This rule prohibits help for a small business "engaged in the creation, organization, expression, dissemination, propagation or distribution of ideas, values, thoughts, opinions or similar intellectual property, regardless of medium, form, or content."

We are also here to discuss a bill which is currently pending before the subcommittee, H.R. 1157.¹ This bill, which was introduced by Representative Joseph Addabbo, would restrict the authority of the SBA to deny financial assistance to small business concerns solely because the primary business operations of such concerns relate to the communication of ideas.

Today we will hear from witnesses who are against the SBA's opinion molder policy and are in favor of this legislation, H.R. 1157. Then early next year we will hold another hearing on this subject. At that time the SBA will testify, as well as legal experts, and parties in favor of the policy.

Let me say at this time that each and every one of you who is testifying today will have a chance to respond to the SBA after they testify. Your comments at that time will be included in the official hearing record, if you so desire.

After we have heard testimony from both sides of the issue, the subcommittee will then decide whether any changes to the rule are necessary.

¹See appendix A, p. 145.

Mr. Roth.

Mr. ROTH. Mr. Chairman, I have a statement that I would like to insert into the record, if I may. For the sake of time, I will not read it.

Mr. IRELAND. Without objection, it will be received.

[Congressman Roth's opening statement follows:]

**OPENING STATEMENT OF HON. TOBY ROTH, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF WISCONSIN**

Mr. ROTH. Mr. Chairman, I appreciate your holding these timely and important hearings today on the opinion molder rule. Clearly, legislative review of this Small Business Administration regulation is warranted.

The opinion molder rule raises important issues. On the one hand, we have a situation where most small businesses can receive Federal assistance, but a small subset in the communications area is excluded by the opinion molder rule. On the other hand, it seems to me that the Federal Government does have a legitimate right in denying assistance to some small businesses. For example, my constituents in Wisconsin would object to Federal grants or loans to a publication advocating the forcible overthrow of the U.S. Government, or to a pornographic movie house. Thus, we must review the question of the opinion molder rule carefully and thoroughly.

If we are to take legislative action on the opinion molder rule, we must carefully review both sides of the issue and walk a narrow line between too stringent an approach and too broad an approach. This hearing should help us determine the right way to go on this complex issue, and I appreciate the chairman's holding this hearing today.

I have talked to many of our colleagues who feel concerned about this issue and I think we're going to be able to give our colleagues in the Congress more of a balanced viewpoint after these hearings, so I congratulate you and thank you for having these hearings.

Mr. IRELAND. Thank you for your comment. I am glad to have you here today.

Mr. Stenholm.

Mr. STENHOLM. Nothing at this time, thank you.

Mr. IRELAND. Mr. Bilirakis.

Mr. BILIRAKIS. Mr. Chairman, thank you.

Your statement and your news release says it all. It tells me at least that this committee should be objective and be openminded and hear every viewpoint on this subject. I certainly find myself with conflicting thoughts on it. My conservative nature says that there probably should be some limitations as far as using taxpayers funds, but at the same time we must remember the first amendment and other freedoms. So, I am going to try to keep an open mind and I expect to learn an awful lot.

I commend you, sir, for having these hearings. Thank you.

Mr. IRELAND. Thank you.

Mr. Daub, glad to have you here this morning.

Mr. DAUB. Mr. Chairman, I would simply like to take a moment to thank the subcommittee and to thank you particularly for your

leadership in undertaking to build a record on these important issues.

I am not a member of the subcommittee. I take an interest in it particularly because I have an interest in H.R. 1157 and in testimony which will be presented by two constituents of mine who reside and work in Omaha, Nebr. On point No. 5 of your agenda you will see Mr. Steven Riekes and Mr. Yale Richards who will testify. Their testimony is of interest to me and I know it will be to this subcommittee. I appreciate the opportunity to at least in that way introduce testimony yet to come before you in this very important matter.

I thank you for your time.

Mr. IRELAND. We thank you, and we thank you for that introduction of your associates. Having been an alumnus, a man with the name of "Yale" can't be all bad, either. [Laughter.]

We will begin then, if there is no further comment, by hearing from Miss Tracey Pinson who is counsel for Representative Joseph Addabbo. Mr. Addabbo is unable to be here this morning because of a previous commitment. Miss Pinson, if you would give us Mr. Addabbo's testimony, we would appreciate it.

OPENING STATEMENT OF HON. JOSEPH P. ADDABBO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK, AS PRESENTED BY TRACEY L. PINSON

Ms. PINSON. Thank you, Mr. Chairman. I would be pleased to read the statement prepared for Congressman Addabbo and I will proceed by reading it as prepared.

I would like to commend my colleague, Mr. Ireland, for holding hearings on H.R. 1157, a bill that I introduced which would ban the SBA administrative policy of denying financial assistance to those small business concerns engaged in the communication of ideas. This policy has been commonly referred to as the opinion molder rule.

The opinion molder rule, found in 13 CFR 120.2(d)(4), expressly prohibits SBA from granting financial assistance to any business engaged in the expression of ideas, values, or opinions.

There are two purported justifications for the rule. One is apparently based on first amendment grounds. SBA has testified in the past that the agency would like to "avoid the appearance of controlling or influencing the freedom of communication and the editorial selection of such communication material." The second reason given by SBA is that the agency doesn't want to be identified in any way with the opinions and ideas expressed by such businesses. By relying on these concerns to justify the denial of a business loan, SBA is jeopardizing the ability to achieve its statutory objective to aid, counsel, and assist the interest of small business concerns. In effect, the opinion molder rule has operated to preclude SBA from promoting small business participation in industries which have been historically predominated by large business concerns.

I must also add that nowhere in the Small Business Act is there a provision which authorizes SBA to deny financial assistance to a small business simply because it communicates ideas or opinions.

The opinion molder rule has been invoked in a number of cases because of an SBA determination that the business has the potential to disseminate and mold public opinion. According to SBA regulations, financial assistance will be denied if the applicant is engaged in the creation, origination, expression, dissemination, propagation or distribution of ideas, values, thoughts, opinions or similar intellectual property regardless of medium, form or content.

This provision has been applied to authors, music composers and lyricists, greeting card companies, publishers of newspapers, magazines, sheet music, and film makers, theatrical producers, musical programs, motion picture theaters, and academic institutions.

On the other hand, SBA has exempted from the opinion molder rule the advertising industry and the broadcasting and cable TV industry because these industries are already regulated by other agencies of the Government. However, these two powerful and pervasive industries are actively engaged in molding social, economic, and political values and the Federal regulation does not pertain to the dissemination or prohibition of particular ideas. In effect, the application of the rule with its exceptions has resulted in allowing financial assistance to some opinion molding businesses and the imposition of an unfair restriction on others. It is my strong belief that a small business should not be penalized solely because it elects to exercise a first amendment right.

Adversely affected small businesses engaged in the communication of ideas have strongly opposed the rule and have criticized SBA's application of the rule as inconsistent and discriminatory.

There is a clearly demonstrated need to legislate an alternative which is consistent with the Small Business Act and responsive to the needs of the small business community.

H.R. 1157 would amend the Small Business Act to restrict the authority of SBA to deny financial assistance to small business concerns solely because the primary business operations of such concerns relate to the communication of ideas. SBA would have the discretion, however, to deny financial assistance to a small business concern if, on the basis of an administrative hearing, it is determined that such assistance will be adverse to a legitimate public interest or used primarily to promote or criticize political or religious ideas.

Of course, this bill would not change any provision of existing regulation which requires SBA to deny financial assistance to businesses engaged in illegal activities.

Thank you, Mr. Chairman.

I might also add that I have been speaking with Mr. Riekes, and Congressman Addabbo would not be opposed to setting forth explicit exceptions to SBA's ability to grant financial assistance to these businesses.

Mr. IRELAND. Thank you very much, Miss Pinson. We are delighted to have you come before us this morning.

Before we move on to our next witness, I would like to call everyone's attention to the fact. Senator Sasser has introduced similar legislation in the Senate. Apparently this is not widely known because it was just introduced last Friday.

Thank you very much.

Ms. PINSON. Thank you, Mr. Chairman.

Mr. IRELAND. Our next witness at this time is Jerome Gordon, special assistant, National Association of Theater Owners, Newport News, Va.

Welcome, Mr. Gordon.

**TESTIMONY OF JEROME GORDON, SPECIAL ASSISTANT TO THE
PRESIDENT, NATIONAL ASSOCIATION OF THEATER OWNERS**

Mr. GORDON. Thank you, Mr. Chairman, gentlemen, ladies.

The National Association of Theater Owners, commonly known as NATO—which is not the NATO that most of us are familiar with—represents approximately 12,000 movie theater screens throughout the United States.

One of our most serious concerns in our organization is the disappearance of the smaller theaters in urban areas and in America's small towns. A lot of them are "mom and pop" theaters. Ours is a problem shared by many other industries, the sad movement toward chain operations and bigness.

It is increasingly difficult for small theater businesses to struggle today against the competition of television, cable TV, cassettes, pay movie channels, over-the-air TV, and the whole electronic explosion which uses motion pictures as their primary fare. To meet this competition, motion picture theaters today, especially now, more than ever before, must maintain attractive and comfortable surroundings. It is very important that they be able to invest in new, modern, state-of-the-art projection equipment and to make their theaters the prime place for the public to see motion pictures.

This updating and modernization necessarily means borrowing money. Many theater owners were bitterly disappointed when they were unfairly put into the opinion molders category. They were denied the SBA help they desperately needed, and they need it today.

Many of these smaller theaters are the only ones in their towns, and every business suffers when the only theater in town closes. A theater is a focal point in the small town. It helps restaurants and every other type of business. When the theater closes, there is a terrific impact on the economy of the whole small town. Not only that, but we are sort of destroying a whole generation of movie goers. When the smaller theaters have to close, then the youngsters growing up get out of the movie habit. They are more encouraged to stay home and watch television rather than go out.

Going to the movies has been a popular habit in the United States for over 70 years, and many of these habits start with youngsters in small towns. The SBA can be of a lot of help to us in keeping these theaters operating.

There are approximately, we figure, 3,000 theaters that would fall into the category of the low grossing or the small town operations. These theaters employ many thousands of people and contribute millions to local, State, and Federal economies.

We feel the SBA is inconsistent in the interpretation of its mission to assist small business in the United States by excluding this important segment of our economy. Please help us to help the small movie theaters. We don't want to lose them; our country needs them. Thank you.

Mr. IRELAND. Thank you very much, Mr. Gordon.

Let me ask my colleagues if they have any questions. Mr. Roth?

Mr. ROTH. Thank you, Mr. Chairman.

As I interpret this legislation, could we say that political newspapers and the like, such as the Daily Worker, could receive SBA help? Is that right?

Mr. GORDON. As I understand it, that is not only correct but makes it even more unfair to the theaters.

Mr. ROTH. Makes it even more unfair for the theaters?

Mr. GORDON. For the theaters to receive SBA loans.

Mr. ROTH. I see.

I appreciate your testimony. I was just thinking—with the stuff that's in the movies nowadays, you had closed your statement saying "our country needs them." I'm not so sure that's correct. Anyhow, that's the wonderful thing about our country: We do have freedom of expression.

Mr. GORDON. I think our country does need the average, legitimate motion picture theater of which our association represents over 12,000.

Mr. ROTH. I think that's a valid statement when you consider, as you mentioned, the small towns in the country. This is a focal point and a place where our people gather, so I think that's a good point.

Thank you.

Mr. GORDON. Thank you, Mr. Roth.

Mr. IRELAND. Mr. Stenholm.

Mr. STENHOLM. No questions.

Mr. IRELAND. Mr. Bilirakis.

Mr. BILIRAKIS. Mr. Gordon, did I understand your response to Congressman Roth's question to be that even though the Daily Worker could receive taxpayers' help, that you feel that is right?

Mr. GORDON. No, sir. No, sir. I just say it makes it even more unfair to the people that I represent. In my opinion, I would say it's not right.

Mr. BILIRAKIS. So you're admitting, then, that there should be some sort of limitations or restrictions?

Mr. GORDON. Yes, sir, but I'm not in a legal position to mention which restrictions there should be.

Mr. BILIRAKIS. But you are saying that there should not be any restrictions as far as theater owners are concerned?

Mr. GORDON. Yes, sir.

Mr. BILIRAKIS. Have these SBA regulations been tested in court as far as you know?

Mr. GORDON. Not to the best of my knowledge, sir.

Mr. BILIRAKIS. Do you know of many instances where small theater owners have made applications to the SBA for financial assistance and have been turned down as a result of this?

Mr. GORDON. As special assistant to the president, one of my duties is to travel throughout the country to our regional associations. We have a national association and we have sort of subchapters, NATO's of Florida and NATO's of different other areas. One of the prime concerns that I hear when I go to these small conventions and small meetings is usually talking to some of the people who operate the smaller theaters. I recently came from a small

convention in the Kansas area and I was approached by two people, one from Kansas and one from Missouri, who were both turned down recently for SBA loans. It is a concern. The smaller theater owners are trying to stay in business and the SBA could be of help.

As I understand it, the SBA's purpose is to try to assist in maintaining small businesses of all types, and we feel like the theaters are being very unfairly excluded.

Mr. BILIRAKIS. Do you feel the legislation introduced by Congressman Addabbo might pass a lot easier if there were some sort of limitations included therein, limitations of the type we have talked about?

Mr. GORDON. I'm not exactly sure I understand the question, sir.

Mr. BILIRAKIS. Well, I'm referring to things like the Daily Worker, communications such as the Daily Worker and other such mediums. Basically, it's a wide-open type of legislation, is it not?

Mr. GORDON. Yes, sir.

Mr. BILIRAKIS. And it would include, then, communication media such as the Daily Worker and others.

Mr. GORDON. I would have to leave the answer to that to my legal counsel, who will follow shortly.

Mr. BILIRAKIS. I realize that.

Mr. GORDON. It is a legal question.

Mr. BILIRAKIS. OK. Thank you.

I have nothing further, Mr. Chairman.

Mr. IRELAND. Thank you, Mr. Bilirakis.

We thank you very much, Mr. Gordon. We will look forward to hearing from your legal counsel later on for those tough questions. Thank you so much.

Mr. GORDON. Thank you.

[The following letter was received for insertion into the record at this point:]



NATO
AFFILIATE
IN THE HEART
OF AMERICA

November 8, 1983

Representative Andy Ireland
United States House of Representatives
B-363-Rapburn House Office Bldg.
Washington D.C. 20512

Dear Representative Ireland:

The United Motion Picture Association represents movie theatres in the states of Missouri and Kansas.

Our small town and independent owners were eligible for SBA funds to improve and modernize their theatres until 5 years ago when the "Opinion Molders Rule" was invoked by administrative order.

There is a desperate need for these exhibitors to have access to SBA financing in order to survive in their limited markets and fulfill a need to their communities.

We strongly urge support of HB 1157 to correct this inequity - discrimination and re-establish the eligibility of motion picture theatres to receive SBA loans!

Thank you for your assistance.

Sincerely,

Dee Brown

Dee Brown
Executive Director



UNITED MOTION PICTURE ASSOCIATION / HOME OF INTERNATIONAL SHOW-A-RAMA

3612 KARNES BLVD. KANSAS CITY, MISSOURI 64111 816/931-2835

Mr. IRELAND. The next witness is Mr. Shelley Feldman, president, National Association of Concessionaires, from Miami, Fla., the great State of Florida. We're delighted to have you here, sir.

TESTIMONY OF SHELLEY FELDMAN, PRESIDENT, NATIONAL ASSOCIATION OF CONCESSIONAIRES

Mr. FELDMAN. Thank you, Mr. Chairman.

I am engaged in business as a consultant and adviser to the overall food service industry, and I am located in Miami, Fla. I am currently serving as president of the National Association of Concessionaires. The National Association of Concessionaires is a national trade association consisting of manufacturers, suppliers, distributors, processors, and concession operators. Our membership manufactures the products and supplies and operates concession stands in motion picture theaters. We sell popcorn and candy and soft drinks, nachos, hot dogs, ice cream, and all the other goodies that you like to eat when you go to the theater.

Our association has approximately 450 member companies who operate over 25,000 concession locations and who employ in excess of a quarter of a million people. Motion picture theaters represented by their concessions provide a very substantial portion of the business of our members. These member companies operate concessions in theaters representing 75 percent of the total theater screens in the United States. That business last year, at the consumer level alone, was approximately \$800 million to \$1 billion.

I am pleased to testify in support of H.R. 1157. This legislation would prohibit the Small Business Administration from arbitrarily excluding motion picture theaters from receiving loan assistance under its opinion molder policy. Under current interpretations of that policy, it is my understanding that motion picture theaters are ineligible for such loans, a situation that seems to me to run contrary to SBA's congressional mandate to promote and assist small business.

I am a small businessman. The majority of the members of my association are small businessmen. Many theater owners are small businessmen. A great many of these small theater owners operate theaters in small towns and in low-income urban areas. These theaters, if they are to survive and have any chance of competing in the marketplace, desperately need renovation and modernization. If they are old, dirty, or run down, they simply don't have a chance to remain in business, let alone compete. For every theater that goes out of business because of these conditions, there are lost sales by manufacturers, suppliers, and operators who make up the membership of my organization.

The small theater owner who needs to modernize and renovate his theater needs loan assistance. He can't just depend on his concession stand all the time to bail him out. There are others who with such help might have a chance of expanding and building new theaters. It is certainly unfair for the SBA to deny this group of small businessmen the benefits that small businessmen in other industries can receive. You will hear from others this morning concerning the legality of the opinion molder policy and the haphazard treatment small theater owners have received from the SBA.

Let me just state that we are talking about legitimate small business people, many small theater owners, many small concessionaires, and we are talking about people who can provide many additional jobs. It seems to me that these concerns are vastly more important than the abstract notions that seem to have haunted the SBA as a justification for its policy. Sales and jobs are much more important than the on-again off-again interpretation by the SBA of its policy in regard to loans to motion picture theaters.

I want to thank you for your attention and we urge your adoption of H.R. 1157.

Mr. IRELAND. Thank you, Mr. Feldman.

Mr. Roth?

Mr. ROTH. Thank you, Mr. Chairman.

I appreciate your very good testimony and I have no questions. I used to work for a man like yourself when I was a kid going to school.

Do you have many concessionaires in Wisconsin?

Mr. FELDMAN. Yes, we have about 9 or 10 companies in Wisconsin that belong to the association. They might not all be strictly operators; they could be suppliers or processors.

Mr. ROTH. Is it possible to get a list of those from you?

Mr. FELDMAN. Sure. I have one right here. I would be happy to give it to you.

Mr. ROTH. Thank you.

Mr. IRELAND. Mr. Bilirakis.

Mr. BILIRAKIS. Mr. Feldman, I, too, by the way, worked my way through school, as an usher in small theaters in my hometown in western Pennsylvania. In those days my dad needed the supplement at home. I have seen, on a visit to my old hometown all of the theaters closed down. I don't know that there's a single theater still alive in my old hometown, and I would hate to see laws that would discourage and there are laws that, discourage those theaters from staying alive. So basically what we're saying is that every theater in the United States is now forbidden from financial assistance from the SBA?

Mr. FELDMAN. Yes, sir.

Let me just add, gentlemen, that we haven't discussed so far—and I haven't seen anything written—about the motion picture theater as a form of entertainment, which I think is probably one of the most tremendous facts about it, I can remember when I was a little fellow during the Depression, right at the end of it, that the motion picture theaters probably did more business at a nickel a person than they did at other times, because people went to the movies to forget about their troubles. They went to the movies for entertainment, not for any other reason. I think it is a tremendous entertainment media that the United States needs.

Mr. BILIRAKIS. I certainly would agree.

Thank you, Mr. Chairman.

Mr. STENHOLM [presiding]. Mr. Daub?

Mr. DAUB. No questions.

Mr. STENHOLM. OK. We will next call John Dawsey, who is president of the Theatre Equipment Association, from Nashville, Tenn. Welcome, Mr. Dawsey.

**TESTIMONY OF JOHN F. DAWSEY, PRESIDENT, THEATRE
EQUIPMENT ASSOCIATION, INC.**

Mr. DAWSEY. Thank you, Mr. Chairman, ladies and gentlemen.

I am executive vice president of Massey Seating Co. of Nashville, and also currently the president of Theatre Equipment Association, which is the national trade association for the manufacturers and dealers of motion picture theater equipment. Our members manufacture, distribute, install, and service all kinds of equipment and supplies that are used in motion picture theaters.

We are pleased to support H.R. 1157 by Congressman Addabbo, which would abolish the opinion molder rule we have been discussing this morning. Our legal counsel, Mr. Riekes, will be submitting testimony on the lack of legal justification for this treatment of motion picture theaters, and this morning I would like to testify and simply give you some facts that would enable you to recognize the economic dimensions of the SBA's refusal to grant loans to the motion picture theater industry. The motion picture theater industry is, we feel, very significant in this country's commerce. Last year about \$3.5 billion were taken in at the motion picture theater box office. Movie attendance was approximately 1.175 billion people.

In the United States there are approximately 18,700 motion picture screens, of which approximately 3,000 are owned by small businessmen. There are approximately 12 employees per motion picture screen. There are literally tens of thousands of persons employed in the production and distribution of motion pictures, and by those who provide ancillary services to theaters, such as members of our association, who provide projectors, screens, sound equipment, lighting, seats, carpets, drapes, signs, ticket machines, and so forth. Mr. Feldman's concessionaires provide the soft drinks and refreshment, popcorn, candy. There are people engaged in advertising and promotion and those who supply the theaters with paper products, uniforms, cleaning supplies, and so forth.

In the equipment industry itself, our association consists of 107 member firms, about half of which are manufacturers and about half of which are dealers. Our members are located throughout the United States and they, too, employ thousands of people. Of course, the welfare of our industry depends on construction, renovation and modernization of existing theaters.

These facts we think clearly demonstrate that the motion picture industry plays a significant role in our economy. We believe also that the industry has great potential in the future and that the small businessman particularly can continue to play an important role in this area. For example, there are still many movie theaters in this country, in the older neighborhoods and small towns, that are aging and need replacement or renovation if they are to survive the competition from large, well-financed chains and from television and other electronic media. But the small theater owner, like any small businessman, needs help to compete. That is why we presume that Congress established the SBA in the first place. We just don't feel it is fair that the SBA should not afford the same loan assistance to owners of small theaters, that other businesses are receiving. These owners are our customers, and anything that

hurts them certainly hurts business of the members of our association.

We feel that if you weigh the economic importance of this industry, including the small businessmen theater owners, and their employees, and the many other businesses which supply and service the motion picture theaters, against the fears of the SBA that it might be involved with controversy, clearly the rightful interest of legitimate American business should prevail.

If it takes legislation such as H.R. 1157 to give the SBA a proper perspective, and it appears to us that it does, then we urge you to enact this bill.

Thank you.

Mr. STENHOLM. Thank you, Mr. Dawsey.

Any questions, Mr. Roth?

Mr. ROTH. I have no questions, Mr. Chairman. I thank Mr. Dawsey for his fine testimony.

Mr. STENHOLM. Mr. Bilirakis.

Mr. BILIRAKIS. Just to thank Mr. Dawsey for taking the time and trouble to come here.

Mr. DAWSEY. Thank you.

Mr. STENHOLM. I express my thanks to you, too.

Mr. DAWSEY. Thank you, sir.

Mr. STENHOLM. Next we will call Steven Riekens, of Richards, Riekens, Brown & Zabin, of Omaha, Nebr., who is accompanied by Mr. Yale Richards.

TESTIMONY OF STEVEN J. RIEKES, ESQ., ACCOMPANIED BY YALE RICHARDS, ESQ., LEGAL COUNSELS TO THE THEATRE EQUIPMENT ASSOCIATION, INC.

Mr. RIEKES. Good morning. My name is Steven J. Riekens, of the law firm of Richards, Riekens, Brown & Zabin of Omaha, Nebr. I am here today with my partner, Yale Richards. We are legal counsels to the Theatre Equipment Association, Inc., the national trade association of manufacturers and dealers of motion picture theater equipment and supplies. We are here in support of H.R. 1157, introduced by Congressman Addabbo, which would abolish the Small Business Administration's so-called opinion molder policy.

I am particularly pleased to be here because I and others have had several years of frustrating and fruitless correspondence with the SBA on this issue, and we're glad for this opportunity to give the issue again more public and congressional scrutiny.

In view of the length of my statement, and in view of what has already been said today, if I am permitted, I would like to condense where possible my remarks.

Mr. STENHOLM. Not only are you permitted, we would encourage it and appreciate it.

Mr. RIEKES. Well, basically, you know what the rule is and you know that it discriminates against whole categories of businesses. It discriminates against them, and the question is, is there any justification for this discrimination? We think not.

In 1980 the Senate held an investigation on this matter, and at that time Senator Robert Morgan said, "This prohibition creates several constitutional problems * * *." That is, the SBA's prohibi-

tion. "First, the SBA has acted to restrict one particular class of applicants from eligibility without statutory basis, and without a demonstration of a compelling Government interest."

The SBA, as far as I know, justifies its policy basically on two grounds. One, it says we have had this policy for a long time. I'm not particularly impressed by that argument; I don't think an invalid regulation becomes valid just because time passes, or that it improves with age.

The real basis for the SBA's policy, as far as I can tell, is that it says, "If we didn't have the policy, we would have to be a censor, and that would probably be unconstitutional."

How much validity is there to that argument? Basically, I don't think that it is a valid argument because no one is asking the SBA, and no one has asked the SBA to my knowledge, to be a censor. The statute envisions the SBA as a lender, and if it started being a lender, that is determining creditworthiness of applicants, I think the constitutional problem basically disappears.

There is an excellent law review article on the subject, in the San Diego Law Review, vol. 19, No. 4, 1982, which I have placed in the appendixes to my remarks. Basically I think that that covers almost all the legal grounds, including the question of the constitutionality. The law review article states that by invoking the Constitution the SBA is presuming a constitutional infringement that may not exist. It says:

The agency has never demonstrated that the loan recipients fear sanction or established any other compelling Government interest which could support such a rule.

Indeed, the law review article, and others, have pointed out that the constitutional argument may go the opposite way. By maintaining the present rule and discriminating against whole classes of business, the SBA is impeding the spirit of the first amendment rather than upholding it. The first amendment enshrines the concept of competition in a free marketplace of ideas. However, by denying financial assistance to communication related small businesses, the SBA deprives the marketplace of their contribution and allows only, in other words, the big fellows to in operate the media industry. By not assisting these small businesses, the marketplace of ideas is restricted, and, in that sense, the idea behind the first amendment is also restricted.

But I think the opinion molder rule by its own terms, by its own various exceptions and interpretations, undercuts any constitutional argument that the SBA has. A classic example is that there is an exception in this policy for commercial broadcasting, radio and television stations, and cable TV systems, under the regulatory jurisdiction of the FCC. If the SBA is correct in citing the Constitution, then how can this exception to its own policy be justified? It seems to me that the Constitution applies just as much to the FCC as it does to the SBA, and if the SBA truly had a constitutional problem, it certainly is not solved by just buck-passing to the FCC.

Now, there is another exception, and that is general book or music stores are eligible, whereas specialty book stores or record stores are not. There are all kinds of problems with this kind of

exception. I mean, how do you decide what is a general store and what is a specialty store?

In connection with this policy there are exceptions saying if you're a wholesaler of books or records, you cannot get a loan. What's the difference and what's the relevance of the difference between a wholesale distributor of some kind and a retailer? What is the difference between a book company that sells only to libraries, that cannot get a loan, and a book company that sells to the general public? Why is the distinction valid? Why is a general book store that might have all kinds of various controversial books, and might have a rack in the back for sexual material, eligible for assistance, and yet somebody who sells books just to ballet students or to law students, can't get a loan? Does that make any sense? I don't think it does.

What is the difference between a general book store and a general movie theater? We don't think there is any difference there, either. The SBA's only justification for that difference is that you can only see one movie at a time. Now, I just can't understand why that's relevant. You can only see one television station at a time, you can only listen to one radio station at a time, but that's OK according to the SBA.

Now, in addition to all these confusing and, I think, meaningless exceptions, is the particular treatment of the movie theater industry. Until 1978, motion picture theaters were eligible to receive loan assistance. In 1978, however, the SBA specifically ruled that motion picture theaters were ineligible to receive assistance. Then in 1980 the SBA reversed its 1978 ruling and used very strong language. It said that the 1978 opinion ignored precedent, and, "was based on an extremely broad and literal interpretation of the opinion molder rule, which is now being expressly disavowed." I attach a copy of that opinion to my statement.

In 1981, the SBA proposed a rule which acknowledged, obliquely, its 1980 opinion, but proposed to disallow certain kind of theaters that show sexually oriented films or advocate philosophical or political ideas. But they never enacted that rule. Then some time later, they took the position that they weren't following the 1980 ruling, or their practice prior to 1978, but were just, in general, ruling movie theaters ineligible again.

Now, it seems to me that kind of record of on-again, off-again, on-again, off-again, shows the depth of uncertainty which the SBA has concerning the validity of its own policy. Further, no group of small businessmen, no segment of American industry, ought to be subjected to that kind of paripatetic policymaking.

Given these inconsistencies and the illogic of and lack of legal foundation for the opinion molder rule, what is the real reason why we have the rule? According to the San Diego Law Review article, the real reason is a bureaucratic one, namely to avoid embarrassment. It states:

The SBA's oft-repeated first amendment justification for the opinion molder rule might represent an attempt to avoid involvement in controversial issues. The agency is unwilling to risk the public outcry which would result if it abolished the rule and assisted qualified opinion-molding small businesses which express unpopular yet constitutionally protected opinions.

I came to the same conclusion, and many others have, too, but I want to stress something. The primary function of the SBA should not be to avoid embarrassment, but it should be to assist all legitimate small businesses.

We believe the only way to remedy this situation is by legislation, and I stress the importance of legislation because, as I said earlier, in 1980 the Senate investigated this subject, and Mr. Harold A. Theiste, Associate Deputy Administrator for Programs of the Small Business Administration, testified before the Senate subcommittee. In his testimony, Mr. Theiste specifically acknowledged the various problems dealing with the opinion molder policy. He stated:

We are aware of recent mergers and acquisitions in the media industry, and we are concerned about the tendency that these takeovers have to eliminate many media-oriented small businesses. We are also concerned that our present opinion molder policy relative to media industry eligibility may be unnecessarily inhibiting our ability to assist these small businesses.

Then he stated they were reviewing the policy in the SBA and would work to make appropriate changes. He stated:

We note that there has been strong sentiment in both Houses of Congress favoring a change in the policy, and we acknowledge that the present policy has produced inconsistent results in the way our assistance has been rendered. Therefore, we have recently undertaken a review of the policy from the legal standpoint, and will soon be prepared to make regulatory changes in the policy which we feel will allow us to make much more assistance available from SBA to media concerns.

But, he argued to give SBA a chance to put its house in order by regulation and not by legislation.

Despite those remarks, the SBA has not followed through and made no changes since that time. Consequently, we believe that legislation is needed with that kind of record.

In this connection, we have drafted a slightly revised bill, keeping the basic intent, but using more precise language. The more precise language includes, by the way, specific mention of motion picture theaters, which is not in the Addabbo bill, and generally tightens the language. Also, this language that we have drafted is extremely similar to the bill introduced by Senator Sasser last Friday.

Before I conclude, I am going to say something that I did not put in my remarks but apparently is on a lot of people's minds. One question came up about the Daily Worker. What if they were to apply for a loan? The other major concern seems to be questions related to pornography.

First of all, in dealing with pornography, the SBA said, in remarks in the Federal Register in 1980, that there is little likelihood, as a practical matter, that businesses dealing in these areas would need assistance. That is the SBA stating this. They said such businesses—sexually explicit magazines, pornographic bookstores and theaters—are generally not in need of governmental assistance.

Second, let's suppose that somebody, whether a sexually oriented business or some extreme group of some kind, did apply for a loan. They still have to be creditworthy. They have to pass all of the other requirements that a lender has. In this connection, one of the things to be taken into consideration is not strictly finance, but if

they're on the borderline of legality. If they're illegal, then SBA has no business loaning them money. If they may be illegal in the jurisdiction in which they operate, or SBA makes a good faith determination that this business is so close to problems in the jurisdiction in which it proposes to conduct its business, that there is a likelihood that it may be shut down, declared a nuisance, or run into some other kinds of legal problems, there is a serious question about its ability to repay its loan, then the SBA can operate to say, "We're not saying you are necessarily illegal or whatever, but we're making a judgment that you're going to have serious problems and as a lender, therefore, we deny your loan."

Next, there is a question of how you control this kind of thing anyway. I would suggest you don't strike a blow against pornography by denying whole classes of otherwise legitimate businesses in the media industry their chance to compete. You don't really do that because under the current policies now of the SBA there is nothing that stops a cable TV network from running all kinds of blue movies, and yet they can get loans. There is nothing stopping a bakery shop from producing pornographic cakes and cookies from springing up, or a T-shirt company from printing whatever they want to on a T-shirt, ostensibly a harmless kind of a business. But they could do that.

Now, what are we going to say? Well, because maybe some bakery might do something like that, or some T-shirt company, or some bookstore might sell whatever, we're not going to loan any of these people any money either, because of what might happen? I don't think that makes sense. I don't think you have controlled the problem that way. This relates to a kind of analysis of balancing the equities and that deals with the Daily Worker issue, too.

The question here is, we have a Government policy based on "what if." What if something should happen? What if some of these people on the fringes should somehow apply? Well, as I said before, these businesses have to pass all credit tests. I don't think we're dealing too much with reality. Even if we are going to say because maybe somebody who we don't care for, or who we don't like, is going to apply, that therefore we're going to just deny thousands upon thousands of legitimate businessmen their rights, and tens of thousands, maybe hundreds of thousands, of workers their jobs? If you place that in any scale, is that an equitable balance? I don't think it is. I don't think it is at all.

It really goes back to the embarrassment issue. There is no way for Government to operate—as you gentlemen should know—and ever hope to say we're going to be free from now on of embarrassment, we're going to think of every conceivable thing that may happen and try to avoid it, to avoid being embarrassed. If the Government were to adopt that kind of philosophy, Government wouldn't do anything at all. I don't think that's the way Government should operate. It is the way the SBA has tried to operate in this field, but it is just not a viable approach to these kind of problems.

Concluding then with the law review, it makes an excellent statement:

Justification for the current opinion molder rule has largely evaporated. The application of the rule has been inconsistent and unfair; the legal basis for the policy

is extremely doubtful and the rule unnecessarily dilutes the agency's effectiveness in strengthening the participation of small businesses in key fields. The SBA should be neither a censor nor a moralizer. Instead, it should be a lender whose priority should be to increase the contribution of small businesses toward the national economy and whose eligibility decision should be based on creditworthiness.

We urge the passage of H.R. 1157 with our suggested amendments. Thank you very much for your attention.

[Mr. Riekes' prepared statement with attachments follows:]

PREPARED STATEMENT OF STEVEN J. RIEKES, Esq.

I am Steven J. Riekas, of the law firm of Richards, Riekas, Brown & Zabin, P.C., of Omaha, Nebraska. I am here today with my partner, Yale Richards. We are legal counsel to the Theatre Equipment Association, Inc., the national trade association of manufacturers and dealers of motion picture theatre equipment and supplies. We are here in support of H.R. 1157, introduced by Congressman Joseph P. Addabbo, which would abolish the Small Business Administration's so called "opinion molder" policy. I am particularly pleased to be here because I, and many others, have spent years in fruitless and frustrating contact with the SBA on this issue. Now, at the very least, the SBA's actions will be opened to more public and Congressional scrutiny.

The SBA's opinion molder policy is a regulation to be found in 13 CFR Part 120.2(d)(4). It prohibits assistance to those

"... engaged in the creation, origination, expression, dissemination, propagation, or distribution of ideas, values, thoughts, opinions or similar intellectual property, regardless of medium, form, or content."

Under this rule, whole categories of legitimate businesses have been excluded from SBA loan assistance. These include authors, composers, newspapers, magazines, publishing companies, motion picture and record producers, schools, theatre groups, the greeting card industry, and those who deal with or distribute these items. Under current interpretations, motion picture theatres are also ineligible to receive assistance.

Is there any legal justification for this discrimination? We think not. In the first place, there is no statutory basis for such discrimination. In 1980, Senator Robert Morgan, then Chairman of the Subcommittee on Government Procurement, Select Committee on Small Business, stated:

"...[T]his prohibition creates several constitutional problems. First, the SBA has acted to restrict one particular class of applicants from eligibility without statutory basis and without a demonstration of a compelling Government interest."

The SBA justifies its policy on two grounds. First, it points out that the policy has been in effect, in one form or another, for many years. However, as an attorney, I am surprised to learn that Government regulations can be analagous to old wine, improving with age. On the contrary, the passage of time does not validate that which is invalid. Furthermore, the inconsistencies in the SBA's application of this rule, over the years, indicate that we have not wine, but vinegar.

Second, the SBA's chief pillar of support is a claim that the policy is needed because, otherwise, there would be problems with the first amendment to the Constitution. The SBA has stated that if it did not have this policy, it would have to decide which ideas were good and deserving of financial assistance, and which ideas were bad and not deserving. Therefore,

"Were the Agency to attempt to make individual decisions on what is, or is not, in the public interest based upon content, it would place itself squarely in a censorship position, which would also not be in the public interest, and which would be unconstitutional." (Letter from Edwin T. Holloway, Associate Administrator, to Senator Jim Sasser, October 6, 1982.)

However, no one is asking that the SBA be a censor, nor is there any reason why it should be. If the SBA made its decisions on the basis of credit-worthiness, its constitutional problem would evaporate.

Furthermore, the Agency believes that if it participates in a loan to an opinion molder, his fear that the SBA might demand early repayment if he expresses a controversial opinion may cause him to alter the content of his expression. While, in making these arguments, the Agency has invoked the sanctity of the Constitution, these arguments are sanctimonious illusions. This has been amply demonstrated in an article in the San Diego Law Review, Volume 19, Number 4, 1982, which I place in the appendices

to this statement. The article points out that this kind of rationale might be "characterized as a kind of presumed prior restraint problem..." But, this rationale is not legitimate. The article states:

"... [N]either the Code of Federal Regulations nor the Small Business Act permit the SBA to recall a loan because of a recipient's opinion molding activities. As a lender, the SBA may demand repayment of the loan only in the event of default."

Further, the rationale

"...[P]resumes a constitutional infringement that may not exist. The Agency has never demonstrated that loan recipients fear sanction or established any other compelling government interest which could support such a rule."

Indeed, by denying assistance to whole classes of legitimate business in the area of communication of ideas, the SBA may be impeding the spirit of the first amendment rather than upholding it. The first amendment enshrines the concept of competition in a free market place of ideas. However, "by denying financial assistance to communication related small businesses, the SBA deprives the market place of their contribution."

The opinion molder rule, by its own terms, also undercuts its own justification. For example, there is an exception for operators of commercial broadcasting (radio and television) stations and cable t.v. systems under the regulatory jurisdiction of the Federal Communications Commission. If the SBA is correct in citing the Constitution, then, how can this exception to its own policy be justified? It seems to me that the Constitution applies just as much to the FCC as it does to the SBA. If the SBA truly had a constitutional problem, it is not solved by passing the buck to the FCC.

In another exception to the opinion molder policy, the SBA allows assistance to "general book or music (record) stores." However, the same section rules as ineligible "specialty stores primarily selling products that promote or advocate ideas..."

There are numerous problems with this exception. How wide a variety of books or records must a store sell in order to qualify as a "general" book or record store? Is not such a distinction subjective, necessarily requiring individual decisions based upon a determination of content? And of what

relevance is such a distinction altogether? Is the general book store that prominently features the latest political exposé or torrid novel somehow less controversial than the speciality shop that only sells books on ballet?

Also, what is the difference between a general book store and a general movie theatre? In a desperate response to this question, the SBA wrote a letter to Senator Jennings Randolph stating that "at any given time", a general book store "passively presents a wide range of topics and titles", whereas, a movie theatre would selectively present an individual work. Why is a moment in time relevant? One can only watch one television station, or listen to one radio station at a time, but that doesn't bother the SBA. On the other hand, one can go to many movie houses that show, simultaneously, six or eight different films. Unfortunately, many deserving businessmen have been victimized by these meaningless and confusing distinctions.

Not only are there internal inconsistencies in the rule, but also the SBA has been inconsistent in its application and interpretation. For example, in our own industry, it appears that prior to 1978, motion picture theatres were eligible to receive loan assistance. In 1978, however, the SBA specifically ruled that motion picture theatres were ineligible to receive such assistance. In 1980, the SBA reversed its 1978 ruling in no uncertain language. It said that the 1978 opinion ignored precedent "... and was based on an extremely broad and literal interpretation of the opinion molder rule which is now being expressly disavowed." I insert a copy of this opinion in the appendices to this statement.

In 1981, the SBA proposed an amendment to the rule which obliquely acknowledged its 1980 opinion that theatres were eligible, but proposed that theatres that show sexually oriented films, or advocate philosophical or political ideas, should be excluded. (Federal Register, Vol. 46, No. 39, February 27, 1981). That rule change was never enacted.

It appears, however, that the SBA has never followed its own 1980 opinion. In correspondence to me, Charles R. Hertzberg, Acting Deputy Associate Administrator for Financial Assistance, stated "...[N]o change will be made in our present policy which prohibits the making of loans to all theatres."

The foregoing visibly establishes the depth of uncertainty which the SBA has concerning the validity of its own policy. No group of small businessmen, no segment of American commerce, ought to be subjected to such peripatetic policy making.

Given the inconsistencies, the illogic of and the lack of legal foundation for the opinion molder policy, what then is the real reason for SBA's insistence on maintaining it? The San Diego Law Review article suggests that the answer is a bureaucratic one, namely, to avoid embarrassment of the Agency.

"The SBA's oft-repeated 'first amendment' justification for the opinion molder rule might represent an attempt to avoid involvement in controversial issues. The Agency is unwilling to risk the public outcry which would result if it abolished the rule and assisted qualified opinion-molding small businesses which express unpopular yet constitutionally protected opinions."

Independently, we came to the same conclusion. However, the primary function of the SBA should not be to avoid embarrassment, but should be to assist all legitimate small businesses.

We believe that the only way to remedy this situation is by legislation such as H.R. 1157. I stress that legislation is necessary because the SBA has been completely unresponsive in this matter. In 1980, the Senate investigated this subject. Mr. Harold A. Theiste, Associate Deputy Administrator for Programs, Small Business Administration, testified before the Subcommittee on Government Procurement of the Select Committee on Small Business, United States Senate.* In his testimony, Mr. Theiste specifically acknowledged various problems dealing with the opinion molder policy. He stated, for example,

"... [W]e are aware of recent mergers and acquisitions in the media industry, and we are concerned about the tendency that these takeovers have to eliminate many media oriented small businesses. We are also concerned that our present opinion molder policy relative to media industry eligibility may be unnecessarily inhibiting our ability to assist these small businesses."

He stated that SBA was reviewing its policy, and would work to make appropriate changes. Then he stated:

"We note that there has been strong sentiment in both Houses of Congress favoring a change in the policy, and we acknowledge that the present policy has produced inconsistent results in the way our assistance has been rendered. Therefore, we have

*(Hearing before the Subcommittee on Government Procurement of the Select Committee on Small Business, United States Senate, Ninety-Sixth Congress, Second Session, on S. 2873, July 24, 1980.)

recently undertaken a review of the policy from the legal standpoint, and will soon be prepared to make regulatory changes in the policy which we feel will allow us to make much more assistance available from SBA to media concerns."

Mr. Theiste argued strongly for the right of the SBA to make a regulatory change rather than for enactment of legislation.

However, despite Mr. Theiste's remarks, the SBA has done absolutely nothing to change its opinion molder policy. Indeed, I submit to you in the appendices to this statement my correspondence with the SBA, which would indicate continued and stubborn unresponsiveness to these problems.

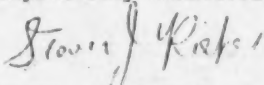
In light of the foregoing, then, legislation is needed. In this regard, we have prepared, and attached to the appendices, proposed amendments to H.R. 1157, which preserves its intent, but is drafted with somewhat more precise language. We understand that Congressman Addabbo has not objected to our suggested revisions. The more precise language is to deal with the SBA's hangups on the issue of religiously oriented businesses, and with such items as obscenity. Incidentally, because a small percentage of theatres may show sexually oriented films, is no reason to ban an entire industry. The SBA ought to assist all legitimate segments of American industry, without discrimination.

Let me conclude by again quoting from the excellent law review article:

"Justification for the current opinion molder rule has largely evaporated -- the application of the rule has been inconsistent and unfair, the legal basis for the policy is extremely doubtful, and the rule unnecessarily dilutes the Agency's effectiveness in strengthening the participation of small businesses in key fields. The SBA should be neither a censor nor a moralizer; instead, it should be a lender whose priority should be to increase the contribution of small businesses toward the national economy and whose eligibility decisions should be based on creditworthiness."

We urge the passage of H.R. 1157 with the suggested amendments.

Respectfully submitted,



STEVEN J. RIEKES

A BILL.

To amend the Small Business Act to restrict the authority of the Small Business Administration to deny financial assistance to small business concerns solely because the primary business operations of such concerns relate to the communication of ideas.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 4(d) of the Small Business Act (15 U.S.C. 633 (d)) is amended to read as follows:

"(d)(1) Except as provided in paragraph (2), the Administration may not deny financial assistance under this Act to any small business concern solely because the primary business operation of such concern is book, newspaper, magazine, greeting card, or calendar publication or distribution; radio or television broadcasting; film, record, or video tape production or distribution; theatre or motion picture entertainment; instruction or tutoring academic subjects; or any other similar operation.

"(2) The Administration may deny financial assistance to any small business concern referred to in paragraph (1) if the Administration determines on the basis of a hearing on the record, that such assistance will be -

"(A) used primarily to advance or inhibit religion, or

(B) used primarily to threaten the overthrow of organized government by unlawful means, or

(C) used primarily to engage in any illegal activity, including without limitation, gambling, or the dissemination of obscene materials, which may be unlawful in any jurisdiction in which said small business concern may operate."

"(3) Any small business concern which is denied financial assistance pursuant to paragraph (2) of this subsection shall be entitled to judicial review in accordance with chapter 7 of title 5, United States Code."

SUGGESTED AMENDMENTS TO H. R. 1157

The following details the changes from the language in H. R. 1157 and the reasons therefore.

1. In Section (1), page 2, line 2, the word "history" has been deleted from before the phrase "calendar publication". Anyone who publishes calendars should be free from the SBA Opinion Molder Rule, whether the calendar deals with an historical theme or any other theme.

2. In Section (1), page 2, line 4, the phrase, "theatre or motion picture entertainment" has been added and inserted after the word "distribution". This addition clarifies the intent of the Section that theatre and motion picture entertainment should also be free from the SBA's Opinion Molder Rule. Over the years, the position of the SBA has been very inconsistent in regard to motion picture theatres. Sometimes they have been included within the rule and sometimes they have been excluded. Since the purpose of this legislation is to abolish the SBA's Opinion Molder Rule in essence, then, this controversy should be ended once and for all by specific language.

3. In Section (2), page 2, lines 10 through 13, the language in sub-clauses (A) and (B) has been changed by substituting new sub-clauses (A), (B) and (C). The purpose of this substitution is to make the language more exact and to more adequately deal with any Constitutional question, particularly in relation to the First Amendment.

The new sub-clause (A), denies assistance to a concern which will use the assistance "primarily to advance or inhibit religion". This phrase is taken from some of the recent court cases and is more precise than the language contained in H. R. 1157.

The new sub-clause (B), denies assistance to concerns who would use such assistance "primarily to threaten the overthrow of organized government by unlawful means". This is better phraseology than the language of H. R. 1157 which eliminates assistance to concerns who would use such assistance "primarily to promote or criticize political ... ideas". That language, in effect, would deny assistance to many newspapers and magazines and the like. There is no reason why these businesses should not be eligible for SBA assistance, except only in the most extreme cases. Therefore, instead, language has been used which would permit the SBA to deny assistance only to those business which would use the assistance "primarily to threaten the overthrow of organized government by unlawful means". This phraseology should eliminate those extremist groups who are beyond

the pale of legitimacy, while at the same time preserving free speech to the over whelming majority of small business concerns engaged in the publication and dissemination of ideas.

New sub-clause (C) denies assistance to those who would use it for any illegal activity. As an example of such illegal activity, both gambling and the dissemination of obscene materials are mentioned. The SBA has, historically, been opposed to assist gambling. Also, by specifically providing that assistance should be denied to those that disseminate obscene material, this should also eliminate the SBA's current hang-up with this issue.

Outside of the foregoing, the rest of the language in H. R. 1157 has not been changed.

The foregoing revisions do not change the intent of H. R. 1157, but merely offer more precise language.

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REVISION OF THE SBA OPINION MOLDER RULE

The Small Business Administration is currently re-evaluating its "opinion molder" rule which bans loan assistance to businesses which promulgate ideas or opinions. This Comment examines the justifications for and application of the rule, contends that it has serious constitutional problems, and proposes an alternative policy which is consistent with the legislative intent of the Small Business Act and more responsive to the needs of the small business community.

INTRODUCTION

The Small Business Administration (SBA) was created by Congress to "aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to preserve free competitive enterprise."¹ The SBA's main function is to administer federal loans to small businesses that are unable to secure other forms of assistance and that demonstrate the potential to exist and grow without government aid, repay the loan, and contribute to the overall economy. Unfortunately, the SBA has a regulatory policy which inhibits its ability to pursue its statutory goal. The so-called "opinion molder" rule precludes many communication-related businesses from loan eligibility and is the source of a current controversy which may lead to a major change in SBA policy.

The rule² prohibits the SBA from granting financial assistance

1. 15 U.S.C. § 631(a) (1976).

2. The rule in use until 1976 banned assistance to any "newspaper, magazine, book publishing company, radio broadcasting company, television broadcasting company, film production company, or similar enterprise." 13 C.F.R. § 120.2(d)(4) (1975). The amended rule, adopted December 21, 1976, states that "financial assistance will not be granted by SBA . . . [i]f the applicant is engaged in the creation, origination, expression, dissemination, propagation or distribution of ideas, values, thoughts, opinions or similar intellectual property, regardless of medium, form, or content." 13 C.F.R. § 120.2(d)(4) (1981). Although the Small Business Act does not specifically mandate the opinion molder policy, the SBA finds legislative authority for its promulgation of the rule in § 204 of the Act. Small Business Act of

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to "opinion molders"—business concerns that promote or advocate ideas, values or opinions. The SBA is not attempting to suppress particular viewpoints which it finds distasteful; instead, it denies loans to any applicant whose business engages in the expression of any opinion.³ "It is immaterial whether the ideas are innocuous or controversial";⁴ the SBA will simply not assist an opinion molder.

The philosophy underlying the rule is twofold. First, the Agency recognizes the first amendment freedoms of loan recipients who operate opinion molding businesses, and wants to avoid being accused of attempting to "control or influence through such loans . . . the freedom of communication and the editorial selection of such communication material."⁵ Second, the SBA refuses to become identified to any degree with the opinions and information selected or distributed by such businesses.

The SBA has defended the rule on several grounds, including the rule's historical background. The SBA's predecessor agency, the Reconstruction Finance Corporation, had adopted a similar policy with respect to its business loans. As early as 1948, the rule appeared to have congressional support.⁶ When the SBA was created in 1953,⁷ its Loan Policy Board adopted the opinion molder rule at its first meeting.⁸

The SBA also contends that the rule "is supported on its merits by a compelling logic":⁹

The exercise of First Amendment rights can be almost as effectively inhibited by the hope of Government assistance as by the fear of Government

1953, Pub. L. No. 83-163, § 204, 67 Stat. 232. This language directs the Administrator of the SBA to establish general policies to govern the granting and denial of applications for financial assistance by the Administration.

3. H.R. Rep. No. 840, 94th Cong., 2d Sess. 27 (1976) (statement of L. Laun).

4. 95 S.B.A. Op. Dig. 100 (1975).

5. 68 S.B.A. Op. Dig. 101 (1968).

6. S. Rep. No. 974, 80th Cong., 2d Sess. 11 (1948):

In the last analysis the determination of whether or not a particular loan will serve the public interest, must be left to the discretion of the Directors of the Corporation.

In the exercise of this discretion, RFC has decided as a matter of policy not to make loans to the press or radio. It cannot be denied that a loan to a newspaper under certain circumstances might serve a very useful public purpose. It is more important, however, for the Government not to become financially concerned with the success of any industry which is engaged in the exercise of our very jealously guarded rights of freedom of speech and press. The committee believes that RFC should have the discretion to make policy decisions of this character.

7. Small Business Act of 1953, Pub. L. No. 83-163, 67 Stat. 232.

8. The opinion molder rule adopted by the first Loan Policy Board of the SBA on September 16, 1953 was expressed in § IV(E)(6) of the Loan Policy Statement, and prohibited financial assistance "if the applicant is a newspaper, magazine, radio broadcasting or television broadcasting company or similar enterprise."

9. H.R. Rep. No. 840, 94th Cong., 2d Sess. 27 (1976) (statement of L. Laun).

sanction. . . . If SBA were to abandon its present policy of nonassistance to disseminators of ideas and values, it would have to develop a substitute policy. Either assistance would be available to all disseminators, without regard to the merits of their ideas; or SBA would have to develop standards to determine which ideas were "good" and deserving of financial assistance, and which were "bad" and hence, undeserving.¹⁰

Despite the simple language of the opinion molder rule,¹¹ it has been difficult to interpret and even more difficult to apply. The difficulty is due to an expansion in the general use of mass communication media, the increasingly specialized communication-related businesses in today's market,¹² and the growing number of products and services that may express opinions.¹³ Nevertheless, the SBA clings to its policy, arguing that other options present even more problems:

Finally, because this ineligibility policy has frequently been questioned, it has been carefully weighed by each SBA Administrator. Despite the temptation to eliminate this negative policy, the alternatives of inhibiting the freedom of expressing or promoting unpopular ideas or opinions, of acting as a censor, or of making Government loans to publishers of "hate" or pornographic material, have resulted in continued affirmation of this ineligibility policy.¹⁴

The rule and its application represent a tension between competing priorities. The SBA's statutory goal is to foster the growth and participation of small businesses in a competitive atmosphere. The opinion molder rule, however, reflects two other government interests: (1) the desirability of avoiding "any possible accusation that the Government is attempting to control editorial freedom by subsidizing media or communication for political or propaganda purposes";¹⁵ and (2) the concern that "constitutionally protected rights of freedom of speech and press ought not to be compromised either by the fear of government reprisal or by

10. *Id.*

11. See *supra* note 2.

12. For example, at one time newspapers and magazines were written, edited, printed and distributed by the same company. Modernly, a newspaper may be written by one company, printed by a second and distributed by a third. It is not clear which of these is (or are) the opinion molder.

13. 13 C.F.R. § 120.2(d)(4) (1981) lists common opinion molders: newspapers, magazines, books, greeting cards, sheet music, pictures, posters, film, tape, live broadcasts, recordings or reproductions of sight, sound or musical programs or products, or theatrical productions.

14. *Hearing Before the Subcomm. on SBA Oversight and Minority Enterprise of the House Comm. on Small Business*, 94th Cong., 1st Sess. 84 (1975) (statement of L. Laun).

15. 45 Fed. Reg. 66,807 (1980).

the expectation of government financial assistance."¹⁶ The SBA compromises its ability to achieve its statutory goal whenever it relies on these interests to justify the denial of a loan. Consequently, the Agency has been unable to promote small business participation where it might be the most socially valuable: in those communication fields which have been traditionally dominated by big business.

In addition to the concern that the Agency is not fulfilling its statutory objective, the constitutionality of the rule is subject to challenge on three grounds: (1) instead of protecting first amendment rights, the rule "may actually be impeding the maintenance of a free press in our society";¹⁷ (2) the amended rule is equally as vague as an earlier version struck down by a New York federal district court as unconstitutionally vague;¹⁸ and (3) although the SBA's classification of certain types of businesses as opinion molders may have a rational basis as required by the doctrine of equal protection, the actual *application* of that classification to particular businesses has proven to be extremely complex, and has resulted in an unfair restriction on some opinion-molding businesses. These three grounds will be explored and supported by examples of the SBA's application of the rule in certain industries. This Comment concludes with a proposal for a revised policy.

FIRST AMENDMENT PROBLEMS

The opinion molder rule has been invoked in a multitude of SBA decisions to preclude assistance to creators of intellectual materials, such as authors,¹⁹ music composers and lyricists,²⁰ newspapers,²¹ magazines,²² radio and television broadcasting companies,²³ and the greeting card industry.²⁴ The rule was later extended to preclude aid to those who come in direct contact with original ideas, have the ability to edit or alter the opinion being expressed, and prepare the material for dissemination to the public. Among the industries affected by this extension are publish-

16. *Id.* at 66,608.

17. *Hearing on S.2873 Before the Subcomm. on Government Procurement of the Senate Select Comm. on Small Business*, 96th Cong., 2d Sess. 2 (1980) (statement of R. Morgan).

18. *Loercher & Feminist Book Mart, Inc. v. SBA*, No. 75 Civ. 5494 (S.D.N.Y. June 1, 1977).

19. 29 S.B.A. Op. Dig. 1(c) (1959).

20. *See* 32 S.B.A. Op. Dig. 100 (1964).

21. 50 S.B.A. Op. Dig. 100 (1963); *see also* 13 C.F.R. § 120.2(d)(4) (1975).

22. 51 S.B.A. Op. Dig. 100 (1963); *see also* 13 C.F.R. § 120.2(d)(4) (1975).

23. 13 C.F.R. § 120.2(d)(4) (1975).

24. 96 S.B.A. Op. Dig. 100 (1975).

ing companies,²⁵ motion picture and record producers,²⁶ schools devoted to academic instruction,²⁷ and little theatre groups which produce and perform plays.²⁸ Furthermore, in a 1974 opinion which has caused some confusion,²⁹ the SBA recognized the importance of distributors in the communications business and struck down their eligibility, thereby eliminating those whose primary function is merely to pass on others' opinions. By denying assistance to these industries, the SBA stifles the ability of small businesses to participate in the communication fields.

The rationale for the opinion molder rule might be characterized as a kind of presumed prior restraint problem. The Agency believes that if it issues a loan to an opinion molder, his fear that the SBA may demand early repayment of its loan if he expresses a controversial opinion may cause him to alter the content of his expression. In other words, the SBA believes it would be inflicting an unconstitutional prior restraint on an opinion molder because of his presumed belief that the government may retaliate if he exercises his right to freedom of speech through his business.³⁰

25. 32 S.B.A. Op. Dig. I(B) (1959).

26. 99 S.B.A. Op. Dig. 109 (1975); 83 S.B.A. Op. Dig. 102 (1971); 73 S.B.A. Op. Dig. 106 (1970).

27. 79 S.B.A. Op. Dig. 110 (1970).

28. 81 S.B.A. Op. Dig. 135 (1971).

29. 94 S.B.A. Op. Dig. 102 (1974).

30. A second but much weaker justification for the policy rests on the argument that the SBA is not suppressing anyone's fundamental right to express protected speech; it is simply denying, due to the greater importance of competing concerns, the privilege of securing a government loan in order to start a business through which that protected speech may be expressed. The deterioration of this line of reasoning is well documented in Van Alstyne, *The Demise of the Right-Privilege Distinction in Constitutional Law*, 81 Harv. L. Rev. 1439 (1968). A stronger argument might be that while every citizen has a fundamental right to free speech, the government has no affirmative constitutional obligation to assist business ventures through which that right may be exercised. Thus, an administrative decision not to assist opinion-molding businesses does not directly infringe on first amendment rights. This argument finds support in several recent United States Supreme Court abortion decisions. Both *Maier v. Roe*, 432 U.S. 464 (1977) and *Harris v. McRae*, 448 U.S. 297 (1980) held that, while a woman has the freedom to choose abortion in certain circumstances, that freedom of choice does not carry with it "a constitutional entitlement to the financial resources to avail herself of the full range of protected choices." *Harris v. McRae*, 448 U.S. at 316. Thus, congressional and state decisions to restrict the availability of public funds for abortions do not impinge on the constitutionally protected freedom of choice. This rationale might be valid if the SBA enforced a blanket prohibition and resisted the temptation to create exceptions for certain opinion molders. The creation of ex-

Two problems deprive this rationale of much of its legitimacy. The first arises from the fact that neither the Code of Federal Regulations nor the Small Business Act permit the SBA to recall a loan because of a recipient's opinion molding activities. As a lender, the SBA may demand repayment of the loan only in the event of default.³¹ Indeed, revocation of a loan due to opinion molding activities would appear to be blatant censorship—the position the SBA wishes to avoid.

A second and more substantive problem with the rationale is that it presumes a constitutional infringement that may not exist. The Agency has never demonstrated that loan recipients fear sanction or established any other compelling government interest which could support such a rule. Litigation addressing such constitutional questions usually involves a balancing of first amendment interests against *concrete* competing government concerns.³² The adjudication of constitutional issues requires the presence of "concrete legal issues, presented in actual cases, not abstractions."³³

The opinion molder rule "may be working inadvertently to the detriment of the first amendment freedoms which we all support."³⁴ Nothing in the Constitution, the Small Business Act, or applicable case law lends support or credibility to the denial of government loans to an otherwise qualified small business simply because it is involved in communicative activities. The Supreme Court has pointed out that there is no counterpart to the religious establishment clause applicable to speech and press.³⁵ Thus, providing governmental financial assistance to communication-related enterprises does not appear to violate the Constitution. Conversely, "the First Amendment does not speak equivocally. It prohibits any law 'abridging the freedom of speech, or of the press.' It must be taken as a command of the broadest scope that explicit language, read in the context of a liberty-loving society, will allow."³⁶ Regulations which infringe on first amendment free-

ceptions within the opinion molder class raises equal protection problems. See *infra* notes 39-114 and accompanying text.

31. 13 C.F.R. § 122.23 (1981).

32. See, e.g., *Young v. American Mini-Theaters*, 427 U.S. 50 (1976) (city supplemented its claim of public interest in preserving the quality of urban life by presenting proof that concentration of adult establishments led to increase in crime, etc.); see also *Stone, Restrictions of Speech Because of Its Content: The Peculiar Case of Subject-Matter Restrictions*, 46 U. Chi. L. Rev. 81, 115 (1978).

33. *Golden v. Zwickler*, 394 U.S. 103, 108 (1969); *Ackerman v. Columbia Broadcasting System, Inc.*, 301 F. Supp. 628, 634 (S.D.N.Y. 1969) (both citing *United Public Workers v. Mitchell*, 330 U.S. 75, 89 (1947)).

34. 126 CONG. REC. 8200 (1980) (introduction of S.2873 by R. Morgan).

35. *Buckley v. Valeo*, 424 U.S. 1, 92 (1976).

36. *Bridges v. California*, 314 U.S. 252, 263 (1941).

doms are strictly scrutinized for reasonable alternatives which might have a less chilling effect on constitutional rights.³⁷

The opinion molder rule appears to ignore two related principles which have long been a significant force in first amendment jurisprudence. The first is the "marketplace of ideas" concept espoused by Justice Holmes in his dissent in *Abrams v. United States*.³⁸ "[T]he best test of truth is the power of the thought to get itself accepted in the competition of the market. . . . That at any rate is the theory of our Constitution."³⁹ *Gertz v. Welch* affirmed the importance of competition in a free marketplace: "Under the First Amendment there is no such thing as a false idea. However pernicious an opinion may seem, we depend for its correction not on the conscience of judges and juries but on the competition of other ideas."⁴⁰ By denying financial assistance to communication-related small businesses, the SBA deprives the marketplace of their contribution. This hardly seems consistent with the broad scope of the first amendment.⁴¹

The SBA also ignores the concept of choice. Providing assistance to any kind of opinion molding business will not automatically and irrevocably mold opinion; the expression may never even be heard. People must choose to be exposed to the types of business typically excluded by the SBA. They must choose to buy a greeting card, go to a movie, or attend a school. Furthermore, businesses such as the greeting card industry do not convey messages from the publisher to the general public; the communication runs from the purchaser of the card to its recipient. By denying funds to these industries, the SBA prevents the exercise of these choices. The United States Supreme Court suggested an alternative to this paternalistic attitude in *Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council*:

37. *Speiser v. Randall*, 357 U.S. 513 (1957); *Community-Service Broadcasting, etc. v. FCC*, 593 F.2d 1102 (D.C. Cir. 1978); see also L. TRIBE, *AMERICAN CONSTITUTIONAL LAW* 591 (1978).

38. *Abrams v. United States*, 250 U.S. 616 (1919).

39. *Id.* at 630 (Holmes, J., dissenting).

40. *Gertz v. Welch*, 418 U.S. 323, 339-40 (1973).

41. Furthermore, the SBA's loan policy disallows financial assistance to those businesses that can secure funds privately (i.e., from family, friends or their own resources) or through non-government financial institutions. As a result, the only persons who can express opinions through their businesses are those who are financially secure enough to proceed without the aid of the SBA. The economically disadvantaged opinion molder is out of luck, and society is deprived of his opinion.

"to assume that . . . information is not in itself harmful, that people will perceive their own best interests if only they are well enough informed, and that the best means to that end is to open the channels of communication rather than to close them."⁴²

The SBA's oft-repeated "first amendment" justification for the opinion molder rule might represent an attempt to avoid involvement in controversial issues. The Agency is unwilling to risk the public outcry which would result if it abolished the rule and assisted qualified opinion-molding small businesses which express unpopular yet constitutionally protected opinions.

VAGUENESS

Prior to 1976, the opinion molder rule banned assistance to a "newspaper, magazine, book publishing company, radio broadcasting company, television broadcasting company, film production company or *similar enterprise*."⁴³ In 1974, the SBA considered whether a bookstore should be classified as a "similar enterprise."⁴⁴ It concluded that a "general bookstore" (i.e., one which stocks almost all subjects and viewpoints) is eligible because it would not involve the SBA in the propagation of a particular set of ideas or values.⁴⁵ This exception was not available, however, to a restrictive or "specialty" bookstore which sells books in a single or limited subject area.⁴⁶

This distinction became the subject of much controversy in *Loercher & Feminist Book Mart, Inc. v. SBA* when the SBA was sued by an applicant desiring a business loan for a feminist bookstore.⁴⁷ The applicant advertised itself as "the largest established retail and wholesaler of strictly feminist and non-sexist children's books,"⁴⁸ apparently rendering it ineligible as a specialty bookstore. When the SBA denied the loan guarantee request, the ap-

42. *Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 770 (1976).

43. 13 C.F.R. § 120.2(d)(4) (1975) (emphasis added).

44. 94 S.B.A. Op. Dig. 102 (1974). This decision also announced that the sale of "newspapers, magazines or books by grocery, drug or other general merchandise stores, or by motels, would not render them ineligible. We would assume that such sales were *de minimis*, i.e., an insignificant part of their gross sales or activities otherwise eligible."

45. "In determining whether a bookstore is a general bookstore, it is relevant to consider whether the store carries in stock (1) a variety of titles; (2) in a variety of fields; (3) from a variety of publishers; (4) including bestsellers (fiction or non-fiction, paperback or hardback)." 98 S.B.A. Op. Dig. 102 (1975) (emphasis original).

46. 95 S.B.A. Op. Dig. 102 (1974).

47. *Loercher & Feminist Book Mart, Inc. v. SBA*, No. 75 Civ. 5494 (S.D.N.Y. June 1, 1977).

48. Letter from E. Benderson, SBA Chief Counsel for Special Litigation to W. Brandt, Asst. U.S. Attorney, S.D.N.Y. (Jan. 23, 1976) (quoting plaintiff's pamphlet).

plicant filed a class action suit in a New York federal district court, alleging that the SBA denied the request "based upon a policy and practice of the SBA to disfavor women on the basis of sex, to disfavor businesses which are 'non-sexist,' and by the SBA's invocation of the 'opinion molder rule,' 13 C.F.R. § 120.2(d)(4) (1975), which plaintiffs allege to be unconstitutional."⁴⁹ Although the court held that the SBA's reason for denying the loan was in fact based on the opinion molder rule and not because of an intent to discriminate, it struck down the rule as unconstitutionally vague:

A statute or regulation is unconstitutional if "men of common intelligence must necessarily guess at its meaning and differ as to its application" *Baggett v. Bullitt*, 377 U.S. 360, 367 (1964). The "opinion molder rule" in effect in 1975 clearly must fall within this definition. Plaintiff was found to fall within the scope of a "similar enterprise." It is impossible to tell from a reading of the regulation that a bookstore would be covered by its prohibitions.⁵⁰

The court also examined the SBA's administrative decisions and interpretations of the regulation and found that SBA attorneys themselves "could not agree how the applicant was covered by the rule."⁵¹

While this case was being decided, congressional opposition to the rule was mounting. Although Congress had never objected to the rationale underlying the rule, it began to inquire about the peculiar application of the rule by the SBA. At a 1975 hearing before the U.S. House of Representatives Subcommittee on SBA Oversight and Minority Enterprise of the Committee on Small Business, the SBA Administrator was questioned about the seemingly unnecessary classification of the greeting card industry as a "similar enterprise."⁵² In 1976, the same House subcommittee

49. *Loercher & Feminist Book Mart, Inc. v. SBA*, No. 75 Civ. 5494 (S.D.N.Y. June 1, 1977).

50. *Id.* at 5.

51. *Id.*

While the majority felt plaintiffs were covered by the rule, they could not agree if plaintiff Feminist Book Mart was a specialty bookstore and denied the loan on that basis, or whether it was a general bookstore, but denied the loan because it was still an opinion molder. While it is clear that the loan was denied because of the SBA's interpretation of this rule, it is just as clear that the rule is unconstitutionally vague. The constitutional standard of vagueness is strictly applied where the statute concerns the regulation of rights protected by the first amendment. *N.A.A.C.P. v. Button*, 371 U.S. 415 (1963).

52. *Hearing Before the Subcomm. on SBA Oversight and Minority Enterprise of the House Comm. on Small Business*, 94th Cong., 1st Sess. 82 (1975) (statement of L. Laun).

concluded:

that SBA's rules and regulations do not adequately state the Agency's policy on this issue. In fact, the regulations merely list examples of ineligible concerns, and broadens its impact by including the term "similar enterprise." The Subcommittee finds that such regulations do not provide the small business community with sufficient notice as to the actual operating restrictions in this area.⁵³

The SBA finally revised the language of the opinion molder rule on December 21, 1976,⁵⁴ "in an attempt to clarify its dimensions—not tighten its restrictions."⁵⁵ Instead of listing ineligible businesses, the current regulations prohibit assistance to any applicant engaged in the "creation, origination, expression, dissemination, propagation, or distribution of ideas, values, thoughts, opinions or *similar intellectual property*, regardless of medium, form or content."⁵⁶ The current regulation enumerates specific exceptions to the prohibition⁵⁷ and also provides a one-sentence explanation of the reason for the rule.⁵⁸ Nevertheless, it is arguable that the current language is just as vague as that used prior to 1976. Furthermore, previous administrative decisions with respect to eligibility continue to apply. Thus, inconsistent opinions rendered under a vague rule persist, and the small business community remains no less confused.

THE APPLICATION OF THE RULE AND EQUAL PROTECTION PROBLEMS

The distinction made between types of businesses in the opinion molder policy has evoked much criticism from Congressional committees.⁵⁹ The objections stem from the SBA's selection of opinion-molding small businesses for treatment different from that accorded non-opinion-molding small businesses. According to one senator, "the SBA has acted to restrict one particular class of applicants from eligibility without statutory basis and without

53. H.R. REP. NO. 840, 94th Cong., 2d Sess. 28 (1976).

54. 41 Fed. Reg. 55,508 (1976) (codified at 13 C.F.R. § 120.2(d)(4) (1977)).

55. 117 S.B.A. Op. Dig. 102 (1980).

56. 13 C.F.R. § 120.2(d)(4) (1981) (emphasis added).

57. The exceptions include commercial printers, publishers of advertising and technical materials, firms providing communications production facilities, broadcasters, and the cable television industry. 13 C.F.R. § 120.2(d)(4)(i)-(v) (1981).

58. "Financial assistance to such applicants is barred in order to avoid Government interference, or the appearance thereof, with the constitutionally protected freedoms of speech and press" 13 C.F.R. § 120.2(d)(4) (1981). Although this sentence does not provide substantial guidance to the applicant, it is at least an improvement over the old version of the rule.

59. See, e.g., *Hearing on S.2873 Before the Subcomm. on Government Procurement of the Senate Select Comm. on Small Business*, 96th Cong., 2d Sess. (1980) (statement of R. Morgan). There have been at least three legislative attempts to abolish the policy: H.R. 2378, 95th Cong., 1st Sess. (1977); H.R. 2725, 96th Cong., 1st Sess. (1979); S.2873, 96th Cong., 2d Sess. (1980).

a demonstration of a compelling Government interest."⁶⁰

It is not clear that a compelling government interest is necessary to justify the rule. Under traditional equal protection analysis,⁶¹ strict scrutiny of legislative or administrative classifications is triggered only when fundamental rights or suspect classes are burdened by the regulation.⁶² Demonstration of a compelling government interest may not be necessary in a business or economic context.⁶³ In evaluating challenged business or economic regulations, United States Supreme Court decisions "presume the constitutionality of the statutory discriminations and require only that the classification challenged be rationally related to a legitimate state interest."⁶⁴ Even if the classification is rational and is delineated in clear language, discrimination in the application of the opinion molder rule may nonetheless constitute a violation of equal protection.⁶⁵ A look at several examples of the SBA's application of the rule is instructive.⁶⁶

Music and Dramatic Arts

The SBA's administrative decisions with respect to the music and dramatic arts industries demonstrate the pitfalls into which the Agency has fallen in attempting to interpret and apply its own rule. These decisions illustrate the hazy lines of distinction that have necessarily been drawn in order to accommodate competing policies.

60. Hearing on S.2873 Before the Subcomm. on Government Procurement of the Senate Select Comm. on Small Business, 96th Cong., 2d Sess. 2 (1980) (statement of R. Morgan).

61. See generally L. TRIBE, AMERICAN CONSTITUTIONAL LAW § 16.6, at 1000 (1978).

62. *Id.* This discussion assumes arguendo that the opinion molder rule does not infringe upon fundamental speech rights.

63. *New Orleans v. Duke*, 427 U.S. 297 (1975).

64. *Id.* at 303.

65. 16A AM. JUR. CONSTITUTIONAL LAW § 802 (1979). "While the mere possibility of arbitrary action, where discretion is vested in an administrative agency, does not render a statute vulnerable to the charge that it denies equal protection of the laws, actual discrimination in administration would violate the constitutional guaranty." *Id.* at 949.

66. These examples demonstrate that the SBA has gone from making a distinction between opinion molders and non-opinion molders to making distinctions within the opinion molder class itself. Because this class by definition expresses opinions, most distinctions will have the appearance of censorship or favoritism. This is the constitutional problem the SBA intended to avoid by adopting the opinion molder rule. See *supra* note 14 and accompanying text.

In a 1964 case, the SBA determined the eligibility of a writer/publisher of music and lyrics.⁶⁷ Rather than draw an analogy between this applicant and the author/publisher of a book, the SBA examined the sheet music material and records presented to it, and ruled that it was "merely entertainment music and [did] not express an editorial policy of the applicant."⁶⁸ The applicant, therefore, was eligible for assistance. In 1975, the Agency admitted its error in that case.⁶⁹ By reviewing the subject matter of the music and finding it to be unobjectionable, the SBA in effect determined eligibility on the basis of content, and thereby directly contravened its noncensorship position.

This opinion raises an important issue, one that is perhaps the basis of many of the SBA's difficulties in uniformly applying the opinion molder rule. Instead of rigidly adhering to its regulation, the SBA deferred to its primary objective of increasing small business participation by considering seemingly ineligible materials and formulating a vague exception where the exclusion of those materials did not seem to serve the purpose of the rule. This practice has created the exceptions that are swallowing the rule.

In another series of opinions related to the arts, the SBA has ruled that the musician who writes music and lyrics,⁷⁰ the little theatre group which produces and performs plays,⁷¹ and the motion picture producer⁷² are all ineligible for assistance. In contrast, the owner of the recording studio whose premises are leased for production of the music,⁷³ the "applicant who provides premises, an auditorium or a theater for entertainment by bands or orchestras,"⁷⁴ the group which leases a theater building to showcase a variety of musical talent, cultural programs, community art groups and art workshops,⁷⁵ and the movie theater owner who merely exhibits films produced by others⁷⁶ are all eligible. In drawing this fine line, the Agency stated:

The ineligibility policy applies to the writer, the publisher, the distributor, or the promoter of mass communication material. The ineligibility policy has not been applied to businesses which assist or supply services to a mass communication industry, and which are not directly involved in the

67. 52 S.B.A. Op. Dig. 100 (1964), *overruled by* 99 S.B.A. Op. Dig. 109 (1975).

68. *Id.*

69. 99 S.B.A. Op. Dig. 109 (1975).

70. 52 S.B.A. Op. Dig. 100 (1964), *overruled by* 99 S.B.A. Op. Dig. 109 (1975).

71. 81 S.B.A. Op. Dig. 155 (1971).

72. 14 S.B.A. Op. Dig. 1(A)(2)(a) (1956).

73. 83 S.B.A. Op. Dig. 100 (1971).

74. 83 S.B.A. Op. Dig. 101 (1971).

75. 92 S.B.A. Op. Dig. 103 (1974).

76. *Id.*

creation, promotion or distribution of the ideas and opinions.⁷⁷

This distinction produces inconsistent results. It is difficult to reconcile the eligibility of a restaurant/club owner who deliberately books Bob Dylan or Joan Baez with the ineligibility of a little theatre group that produces "Snow White." The club owner did not "create" Joan Baez' political views, but he is certainly promoting and distributing them. He has the ability to select musical acts for booking, and in that sense is just as effective an opinion molder as is the book publisher or movie producer. Furthermore, the distributor concept in itself is troubling. Although a "distributor of mass communication material" was declared ineligible in 1974,⁷⁸ it is not unreasonable to equate a club owner, a movie theatre owner or the cable television industry (all of which are currently eligible) with a "distributor" of opinion-molding material.

The Advertising Industry

In a series of disturbing opinions, the SBA has excepted from its prohibition the quintessential opinion molder: the advertising industry. According to the SBA, the general ban on financial assistance "has never included advertising publications . . . (i.e., publications consisting solely of advertisements with no editorial material intended to be of an entertaining or informative nature apart from the advertisements themselves). . . ."⁷⁹ In addition to assisting advertising magazines, the SBA will also assist an advertising agency "that does no public relations work,⁸⁰ advertising for political candidates, or other opinion molding,⁸¹ as that term is

77. 83 S.B.A. Op. Dig. 100 (1971).

78. 94 S.B.A. Op. Dig. 102 (1974).

79. 63 S.B.A. Op. Dig. 104 (1974).

80. "Public relations work" has been vaguely distinguished from advertising through the use of the following two examples: "An advertising campaign whose theme is 'vote for X' or one dedicated to the proposition that 'our stockholders are just plain folks' would represent ineligible opinion molding." 104 S.B.A. Op. Dig. 108 (1977). Although the first example is obviously political and its exclusion is consistent with the spirit of the opinion molder rule, the second example is arguably advertising, which is eligible.

81. The Agency later softened its stance:

It would not be inconsistent with our opinion molders' policy to apply a *de minimis* test to determine whether a given advertising agency is eligible for SBA financial assistance; that is, a commercial advertising agency is presumptively eligible for SBA financial assistance, whether it creates the advertising material or merely functions as a media broker, unless a significant amount of its work consists of noncommercial advertising.

Id. (emphasis original).

commonly understood. . . ."⁸²

Although the United States Supreme Court has commented on the significance of accurate commercial speech in promoting an informed society,⁸³ it has not given commercial speech the same degree of protection as political speech.⁸⁴ It appears that the SBA is dangerously underestimating the power of advertising to mold social, economic and political values. The SBA's blanket statement of eligibility ("while opinion molding in one sense is an inevitable objective of any advertising agency, it is not the kind of opinion molding that would make the agency ineligible for SEA financial assistance"⁸⁵) is hardly persuasive enough to justify the special treatment given to the advertising industry. The essential objective of advertising is the molding of opinions.

The exception for advertising publications and agencies was articulated in the SBA's 1976 amended regulations.⁸⁶ A comment in a 1977 opinion illustrates the irony of the rule:

The availability of the "advertising" exception . . . does not depend on the nature of the goods or services for which the applicant prepares or places advertising. Advertising to induce the public to see a particular movie, or to subscribe to a certain magazine, or to attend a particular college, is no less permissible as far as eligibility is concerned as attempting to induce the public to use a particular kind of toothpaste.⁸⁷

The movie, the magazine and the college are all ineligible for SBA assistance because they have the potential to disseminate and mold opinion. Nevertheless, the advertising agency, which is paid by the ineligible concern to convince the public to see, read or at-

82. *Id.* Whether there is a "common understanding" of the definition and dimensions of the term is highly debatable.

83. "As to the particular consumer's interest in the free flow of commercial information, that interest may be as keen, if not keener by far, than his interest in the day's most urgent political debate." *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 763 (1976).

84. Indeed, a plurality of the United States Supreme Court explicitly reaffirmed a statement in *Central Hudson Gas v. Public Serv. Comm'n*, 447 U.S. 557, 562-63 (1979), that "[t]he Constitution . . . accords a lesser protection to commercial speech than to other constitutionally guaranteed expression." *Metromedia, Inc. v. City of San Diego*, 453 U.S. 490, 507 (1981). *But see* *Lehman v. City of Shaker Heights*, 418 U.S. 298 (1973) (United States Supreme Court upheld municipal policy which permitted commercial advertising but disallowed political advertising inside city transit buses).

85. 98 S.B.A. Op. Dig. 101 (1973).

86. 13 C.F.R. § 120.2(d)(4):

Provided, however, that nothing herein shall preclude financial assistance to any otherwise eligible applicants engaged in . . .

....

(iii) *Advertising and technical material*: Firms producing advertisements and promotional material for a client's goods or services, or of technical or instructional material relating to such goods or services.

87. 105 S.B.A. Op. Dig. 104 (1977).

tend its "opinion molder" is eligible.⁸⁸

Broadcasting and Motion Pictures

Opinions pertaining to the broadcasting and motion picture industries best exemplify the equal protection problem. In these industries the unfair application of the opinion molder is most evident, resulting in the eligibility of two powerful and pervasive industries while other qualified, similarly situated industries remain ineligible for assistance.

When the SBA first considered the eligibility of the skyrocketing cable television industry,⁸⁹ its regulations specifically denied assistance to over-the-air television (and radio) broadcasting companies. Seizing the opportunity to increase the participation of small business concerns in the broadcasting industry, the SBA exempted cable television from the general prohibition against broadcasting. The exception only applied to those cable television stations which were "merely passive receivers and transmitters of broadcast signals," those stations which did not "originate or exercise selective judgment for programs transmitted over its cable system."⁹⁰ Thus, a cable television station which had no control over its program content was eligible, while a station with a channel or the capability of live broadcasting was ineligible. Furthermore, the SBA announced that it would require an agreement that the borrower would not offer or install a live television channel while the loan was outstanding.

The eligibility of cable television companies is confusing. In terms of capacity to mold opinion, it makes no sense to distinguish a cable television station from a television station with live broadcasting capacity. The inability of a cable television station owner to originate programming or exercise selective judgment over the programs broadcast does not reduce the opinion-molding effectiveness of the programming in general.⁹¹

88. The SBA also summarily dismissed the advertising agency's participation in the creative and/or editorial process in connection with the preparation of advertising material by begging the question—because the agency creates and edits eligible material, the prohibition against those two processes has no application. 105 S.B.A. Op. Dig. 103 (1977).

89. 75 S.B.A. Op. Dig. 103 (1969).

90. *Id.*

91. The SBA was not unaware of the apparent contradiction in its reasoning. A subsequent opinion stated:

If we were examining this question for the first time today, we would

The SBA repeated its warning that the "present exception in favor of passive CATV must be narrowly construed"⁹² in 1976, but that policy did not last long. In 1977, the SBA exempted from the prohibition not only all cable television companies but *all* otherwise qualified applicants for the purchase or construction of broadcasting stations (radio or television) or cable television systems.⁹³ The Federal Communications Commission's regulation of the industry relieved the SBA of one of the major reasons for previously invoking the opinion molder rule: the first amendment rights of those who run the industry are *already* curbed. Two problems, however, remain with this revised policy: an SBA loan to a broadcaster could still easily prompt an accusation that the government is attempting to control editorial freedom by subsidizing the media for political or propaganda purposes; and, by exempting the entire broadcasting industry while continuing to include newspapers, magazines and publishers within the prohibition, the SBA is unfairly restricting financially qualified, similarly situated, opinion-molding industries that are not "fortunate" enough to be regulated. The SBA's ability to hide behind a layer of governmental regulation has resulted in the eligibility of a pervasive industry; other less powerful but unregulated opinion-molding industries, however, are still bound by the ban.

Early SBA decisions concerning the motion picture industry reflected the idea that the motion picture producer⁹⁴ and the film-strip producer⁹⁵ were ineligible as engaging in a "similar enterprise," based on their ability to exercise "artistic and editorial judgments in order to illustrate, emphasize and dramatize the film's message."⁹⁶ Similarly, an importer of foreign films whose "selection of which films to import involves a discretionary judgment similar to that exercised by a publisher in deciding which books or material he will be engaged in publishing" was ruled ineligible.⁹⁷ Even those producers whose movie scripts were pro-

probably not consider any TV cable system eligible for SBA assistance. We would have to place them in the same category as any other radio or television broadcaster or distributor, i.e., ineligible as a distributor of opinion molding material. (See 94 S.B.A. Op. Dig. 102). It is not clearly consistent with this latter opinion for passive TV distribution to be eligible. However, in view of the eligibility precedent restated in 75 S.B.A. Op. Dig. 103, we have no legal objection to the continuation of the exception for passive cable TV. We do not believe, however, that it would be legally acceptable for this exception to be further extended.

92. S.B.A. Op. Dig. 101 (1975) (emphasis original).

93. 101 S.B.A. Op. Dig. 102 (1976).

94. 42 Fed. Reg. 58,538 (1977) (codified at 13 C.F.R. § 120.2(d)(4)(v) (1979)).

95. 14 S.B.A. Op. Dig. 1(A)(2)(a) (1966).

96. 92 S.B.A. Op. Dig. 103 (1974); 84 S.B.A. Op. Dig. 107 (1972).

97. 83 S.B.A. Op. Dig. 102 (1971).

98. 59 S.B.A. Op. Dig. 100 (1965).

vided by clients were ruled ineligible.⁹⁸

In the midst of this broad base of ineligibility, two exceptions emerged. The first involved a special SBA program, the Small Business Investment Companies (SBIC) program. An SBIC is a privately owned and operated, income-producing enterprise which is licensed, regulated and financed by the SBA.⁹⁹ The SBIC in turn selects and finances a portfolio of small businesses, including "small business concerns which deal in mass media publication or opinion molding."¹⁰⁰ The result is another example of "layering." The SBA stresses the fact that it has no control over the financing decisions made by the SBIC. The SBICs "are independently owned and operated, . . . make their own investment judgments, and are, therefore, free from any accusation of government or political control or suppression as a result of their loan-making activities."¹⁰¹ Nonetheless, the SBICs do operate within a specific set of regulations¹⁰² that impose content restrictions on the projects which the SBICs are allowed to finance.¹⁰³ The inconsistency emerges once again: the SBA, stifled by its own rule from furthering its statutory goal, hides behind an "independent enterprise," claims it has no control over the content of the opinion expressed, and ends up assisting the opinion molder in a roundabout way.¹⁰⁴

The other exception involved the eligibility of motion picture theaters. Early opinions with respect to theaters employed a rationale similar to the one used for restaurant/club owners who book bands or orchestras for entertainment.¹⁰⁵ These opinions held that those who merely exhibit films produced by others were eligible.¹⁰⁶ This reasoning fails for the same reason as was

98. 83 S.B.A. Op. Dig. 102 (1971), 78 S.B.A. Op. Dig. 106 (1970), 59 S.B.A. Op. Dig. 100 (1965).

99. See generally 13 C.F.R. § 107 (1980).

100. 45 Fed. Reg. 66,808 (1980); see also 42 Fed. Reg. 60,729 (1977) (introduction of a pilot program allowing SBICs to invest in motion pictures).

101. 45 Fed. Reg. 66,808 (1980).

102. 42 Fed. Reg. 60,729 (1977), amended by 43 Fed. Reg. 21,439 (1978).

103. For example, 43 Fed. Reg. 21,441 (1978) states that "pilot SBICs will be prohibited from making any investments related to the production or distribution of X-rated or unrated films regardless of the method of their exhibition . . . or of films having a predominant theme of a political or religious nature."

104. For a more comprehensive treatment of motion picture financing by SBICs, see Holmes, *Investing in Independent Motion Pictures Through Small Business Investment Companies*, 13 U.C. DAVIS L. REV. 955 (1980).

105. 83 S.B.A. Op. Dig. 101 (1971).

106. 82 S.B.A. Op. Dig. 103 (1974), 81 S.B.A. Op. Dig. 155 (1971).

pointed out earlier: the "mere exhibitor" is just as able to exercise selective judgment in choosing the films shown at his theater and is just as powerful an opinion molder as the newspaper, magazine or publisher.¹⁰⁷

In 1978, however, the SBA overruled its prior theater decisions in light of its 1976 amended regulations and its "distributor" opinion:¹⁰⁸ "motion picture theaters come within the general prohibition of Section 120.2(d)(4) of SBA's Regulations and are therefore *ineligible* to receive SBA financial assistance. . . . Indeed, a motion picture theater is a '[distributor] of communications, including . . . pictures . . . ' pursuant to subsection (ii) of Section 120.2(d)(4)."¹⁰⁹

The status of motion picture theaters must have caused great consternation at the SBA. While two prior opinions specifically declared them eligible, the rather sweeping language of the amended regulations and the troublesome "distributor" concept threatened to preclude eligibility. With its commitment to increased small business participation at stake, the Agency once again shifted course.

In 1980, the Administration announced the reversal of the 1978 theater ineligibility opinion.¹¹⁰ It declared that equating a motion picture theater with a distributor was interpreting the regulation's language too broadly and unfairly restricting small businesses which had previously been eligible under the old version of the regulations. Thus, the SBA returned to its original position. Motion picture theaters are once again eligible for assistance. The SBA must now confront its worst fear: "making Government loans to publishers of 'hate' or pornographic material."¹¹¹ Ironically, the opinion molder rule, which was intended to preclude this precise possibility, still exists.

CONCLUSION

These examples of the SBA's application of the opinion molder rule furnish a factual basis for deciding whether the doctrine of equal protection has been violated on the basis of discriminatory administration. Something more than mere error of judgment of officials is required to sustain such a charge. "There must be

107. See *supra* note 76 and accompanying text.

108. 94 S.B.A. Op. Dig. 102 (1974).

109. 111 S.B.A. Op. Dig. 104 (1978) (emphasis added).

110. 117 S.B.A. Op. Dig. 102 (1980).

111. *Hearing Before the Subcomm. on SBA Oversight and Minority Enterprise of the House Comm. on Small Business, 94th Cong., 1st Sess. 84 (1975)* (statement of L. Laun).

something more—something which in effect amounts to an intentional violation of the essential principle of practical uniformity."¹¹² "[A] discriminatory purpose is not presumed; there must be a showing of 'clear and intentional discrimination.'"¹¹³ No accusation of purposeful discrimination is being leveled at the SBA, and it is doubtful one could be proven. Indeed, the *Loercher* case is a good example of a court's refusal to find such requisite intent.¹¹⁴ The language of the SBA's opinions reflects a desire to assist as many small businesses as possible. Nonetheless, the decisions also reveal the Agency's hesitance to subject itself to public criticism. The importance of the Agency's statutory goal and the needs of small business concerns demand a bolder approach by the SBA.

PROPOSAL

In a recent advance notice of proposed rulemaking,¹¹⁵ the SBA announced its intent to make major revisions in the opinion molder policy, and solicited public comment regarding seven different plans for modifying the rule. The seven options vary in their degree and manner of retreat from the present policy.¹¹⁶

112. *Sunday Lake Iron Co. v. Wakefield*, 247 U.S. 350, 353 (1917).

113. *Snowden v. Hughes*, 321 U.S. 1, 8 (1943) (citing *Gundling v. Chicago*, 177 U.S. 183, 186 (1899)).

114. *Loercher & Feminist Book Mart, Inc. v. SBA*, No. 75 Civ. 5494 (S.D.N.Y. June 1, 1977).

115. 45 Fed. Reg. 66,807 (1980). On July 24, 1980, the SBA reported the same decision to the United States Senate Subcommittee on Government Procurement of the Select Committee on Small Business:

We are aware of recent mergers and acquisitions in the media industry, and we are concerned about the tendency that these takeovers have to eliminate many media-oriented small businesses. We are also concerned that our present opinion molder policy relative to media industry eligibility may be unnecessarily inhibiting our ability to assist these small businesses. . . . We feel that the time has come for a complete revision of the opinion molder policy.

Hearing Before the Subcomm. on Government Procurement of the Senate Select Comm. on Small Business, 96th Cong., 2d Sess. 5 (1980) (statement of H. Theiste).

116. Briefly summarized, the seven alternatives and their rationales are as follows:

- (1) Retain the present rule, but provide a waiver procedure by which media concerns denied assistance could demonstrate that the purpose of the rule is not served by the denial of assistance.
- (2) Expand the exceptions in the current rule to allow SBA assistance to those types of businesses that meet the present broad definition of an opinion molder, but that do not primarily mold opinions, and the funding of which would not be likely to promote governmental interference with freedom of speech and press.

The following proposal, however, goes one step beyond those outlined in the advance notice. The SBA should consider a rule which allows all small businesses to be eligible, except those to which the grant of assistance would constitute a violation of the religious establishment clause of the first amendment.¹¹⁷

Under this proposal, the SBA would be forced to approve loans to qualified businesses that deal in materials which are sexually

This proposal would eliminate many of the case-by-case determinations involved in the waiver procedure described above.

(3) Replace the present broad proscription against assisting opinion molders with specific prohibitions against certain types of enterprises. This proposal appears to be a reversion to the original language of the rule.

(4) Prohibit SBA assistance to certain forms of media enterprises which advocate a particular religious, political, social or economic point of view. Retraining from assisting all such businesses (regardless of what point of view is advocated), while funding other media concerns which do not advocate a particular point of view, would reasonably accommodate SBA's desire to assist eligible media enterprises while avoiding actual or apparent government censorship of the media.

(5) Prohibit SBA assistance to an applicant if more than thirty percent of the applicant's annual gross income is derived from the sale, rental, or lease of religious products, materials or services. The SBA contends that the thirty percent income limitation contained in the proposal is a reasonable standard by which SBA could determine that assisting an enterprise would violate the first amendment.

(6) Prohibit SBA assistance to an applicant if more than thirty percent of the applicant's annual gross income is derived from the sale, rental or lease of sexually explicit products, materials or services.

(7) Prohibit direct SBA loans to opinion molders. Presently, all financial assistance, including SBA loan guarantees as well as direct loans, are denied to opinion molders. The dangers of government interference with freedom of speech and press is greatest where direct loans are involved. This proposal would be a reasonable accommodation between SBA's desire to assist eligible media enterprises while minimizing the danger of actual or apparent government censorship of the media.

For a more detailed description of the proposed alternatives, see 45 Fed. Reg. 66,806 (1980).

117. "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof . . ." U.S. CONST. amend. I.

The exception to the proposed regulation is necessary because a loan to a religious-oriented business or school could be construed as "sponsorship, financial support, and active involvement of the sovereign in religious activity," *Lemon v. Kurtzman*, 403 U.S. 602, 612 (1971) (citing *Walz v. Tax Comm.*, 397 U.S. 664, 668 (1970)), all of which are prohibited by the establishment clause of the first amendment. The Supreme Court, in *Committee for Public Education and Religious Liberty v. Nyquist*, 413 U.S. 756 (1972), summarized the "well-defined three-part test" used in evaluating the constitutionality of laws which aid religious institutions: "first, [the law] must reflect a clearly secular legislative purpose; . . . second, [it] must have a primary effect that neither advances nor inhibits religion; and, third, [it] must avoid excessive government entanglement with religion." *Id.* at 772-73. While any encouragement of small business participation is clearly a secular purpose, the propagation of religious tenets which would result from a loan to a religious-oriented business might be considered a "primary effect that . . . advances . . . religion," and the length and continuous servicing of the loan by the SBA could be construed as "excessive government entanglement." The only problem inherent in this exception is the determination of exactly what constitutes a "religion" or "religious activity," but this problem is common in first amendment law.

explicit but not legally obscene,¹¹⁸ such as adult theaters, bookstores and shops. Although the SBA and the majority of the American public may find it offensive and indecent, this expression is protected by the first amendment. Recent United States Supreme Court cases have struck down laws which discriminate against certain types of protected speech based on the content of the opinion expressed.¹¹⁹ Government may not grant the use of a forum to people whose views it finds acceptable, but deny use to those wishing to express less favored or more controversial views.¹²⁰ It is arguable, however, that the SBA is again presuming the existence of a problem which may never materialize. This proposal will not make these or any other businesses automatically eligible for assistance. Other SBA eligibility criteria, such as size, inability to secure assistance elsewhere and creditworthiness, must still be satisfied. The SBA itself pointed out in its notice of proposed rulemaking that "hard-core sex industries . . . are generally not in need of governmental assistance and thus SBA's finite resources could be more productively applied to other types of businesses."¹²¹

118. The SBA's regulations have historically contained a provision prohibiting the Agency from assisting an illegal enterprise. 13 C.F.R. § 120.2(d)(9) (1981). Therefore, the SBA would clearly be justified in denying a loan to a business which creates or distributes materials which are determined legally obscene in light of "contemporary community standards." *Roth v. United States*, 354 U.S. 476 (1956). The SBA would also be justified in procuring an agreement from all loan recipients that the production of obscene materials will result in an immediate liquidation of the loan. Such an agreement would not be an unconstitutional prior restraint on protected speech because obscenity is not protected.

119. See, e.g., *Grayned v. Rockford*, 408 U.S. 104 (1972); *Police Dep't of Chicago v. Mosley*, 408 U.S. 92 (1972).

120. *Police Dep't of Chicago v. Mosley*, 408 U.S. 92 (1972).

121. 45 Fed. Reg. 66,809 (1980). An examination of the future of obscenity law is beyond the scope of this Comment. It is worth noting, however, that two recent Supreme Court decisions, *FCC v. Pacifica Foundation*, 438 U.S. 726 (1978) and *Young v. American Mini-Theaters*, 427 U.S. 50 (1976), have received much attention. In *Young*, four Justices agreed that "even though . . . the First Amendment will not tolerate the total suppression of erotic materials that have some arguably artistic value, it is manifest that society's interest in protecting this type of expression is of a wholly different, and lesser magnitude than the interest in untrammelled political debate. . . ." 427 U.S. at 70 (emphasis added). Similarly, in *Pacifica*, the Court hinted that patently offensive but nonobscene materials might not be entitled to full protection: "the constitutional protection accorded to a communication containing such patently offensive sexual . . . language need not be the same in every context. It is a characteristic of speech such as this that both its capacity to offend and its 'social value' . . . vary with the circumstances." 438 U.S. at 746-47. Although both cases have been described as aberrations, see, e.g., Farber, *Content Regulation and the First Amendment: A Revisionist View*, 68 GEO.

There is substantial justification for a complete revision of the opinion molder policy. The rule as drafted and interpreted by the SBA has not been and cannot be consistently applied. Because it is reasonable to assume that the number and scope of communication-related businesses will increase as time passes, it is also reasonable to assume that the SBA's task will become even more complex should it retain the rule.

The current opinion molder policy should be replaced with a rule that furthers the purpose of the Agency rather than one that hinders it; one which would assist small businesses in all fields, particularly those areas in which the previous policy has indirectly promoted big business concentration, such as newspapers and magazines. Aggressive small businesses can provide diversity and innovative competition, which gives established businesses the incentive to lower prices and develop better products. A loan policy that encourages these small businesses seems more consistent with the goal of the SBA than a policy which threatens their existence. Justification for the current opinion molder rule has largely evaporated—the application of the rule has been inconsistent and unfair, the legal basis for the policy is extremely doubtful, and the rule unnecessarily dilutes the Agency's effectiveness in strengthening the participation of small businesses in key fields. The SBA should be neither a censor nor a moralizer; instead, it should be a lender whose priority should be to increase the contribution of small businesses toward the national economy and whose eligibility decisions should be based on creditworthiness.¹²²

With the SBA's proposed revision of its opinion molder rule yet to be announced, one can only guess at the method it will adopt to modify its stance. At the very least, the proposal should demonstrate that the Agency has recaptured its identity as a lending agency, and is on the road to achieving its statutory goal by fully serving all qualified small businesses.

JULIANNE B. D'ANGELO

L.J. 727 (1980), they may provide a clue as to the opinion and direction of the Court concerning nonobscene erotica. Thus, there is some hope for the SBA in its desire to avoid assisting these businesses.

122. It could be argued that a "creditworthiness" decision which involves a determination of the potential marketability of a product or service is inherently subjective and may be tainted by the decision-maker's values. It should be remembered, however, that a "creditworthiness" determination would also consider other weightier factors, such as personal and business credit ratings, personal and business income tax returns, a projection of future sales and expenses, and (for existing businesses) a balance sheet and profit and loss statement.

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February 10, 1982

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AREA CODE 402

OUR FILE NUMBER

Administrator
 Small Business Administration
 1441 "L" Street N.W.
 Washington, D.C. 20416

Dear Sir:

We are attorneys for Theatre Equipment Association, Inc., the national trade association of the theatre equipment industry.

For several years, those engaged in our client's industry and related industries, have been concerned about the ineligibility of motion picture theatres to obtain loans from or guaranteed by the Small Business Administration under your so-called "opinion molder" policy contained in 13 CFR Part 120.2(d)(4). Consequently, we greeted with pleasure, the news that the SBA had published a proposed amendment to these rules, on February 27, 1981, which would have allowed motion picture theatres to become eligible. We were not aware of the proposed rule in time to meet the official deadline for comments.

Concern, however, replaced joy when month after month passed by with apparently no action taken on this proposed rule change. Now, dismay has replaced concern. In the January 8th edition of "News & Views", a bulletin of the National Association of Theatre Owners, the following is said:

" According to Small Business Administration (SBA) officials, the agency plans to drop a proposed rule-making of last February that would have reinstated motion picture theatre eligibility for SBA financed loans. If adopted, the proposal would have reversed a 1978 decision that classified theatres as 'opinion molder' businesses, thereby barring them from SBA financial assistance."

We sincerely hope that the foregoing news is in error, or, if not, that you will reverse these plans and enact the proposed rule change announced last February.

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We find the present exclusion from eligibility of motion picture theatres to be arbitrary, illogical and without proper justification.

As a matter of law, we question the entire so-called "opinion molder" policy, which excludes, wholesale, large segments of American commerce from eligibility for SBA loans. We can find nothing in the statutes which would indicate that Congress has given any authority for such a position. While, admittedly, the SBA has general rule making authority, that is not a blank check to discriminate against whole classes of businesses. Discretion may be appropriate to determine those business that are small and those that are not, and those particular applicants that may be sound credit risks and those that are not; but, we see no right to discriminate against the motion picture industry any more than against people involved in the grocery business, or businesses located west of the Mississippi or for other such reasons. The opinion molder policy is simply not relevant to whether or not a particular business should be given a loan.

What is the rationale for the opinion molder policy? In discussing this with SBA officials in the past, and in reviewing material that has been sent to us, we have heard or seen only oblique references to certain "First Amendment" problems. However, we have been unable to discern any real constitutional or legal issues. We suspect that the real "problem" is not of law, but one of public relations. In other words, the opinion molder policy appears to be aimed at excluding from eligibility for loans, all those who deal with ideas, values, thoughts or opinions, in order to avoid criticism or embarrassment for the SBA. Obviously, it is conceivable that a certain publisher or movie producer, or the like, might be engaged in the dissemination of controversial material, and should such a business apply for a loan, any action the SBA takes might be controversial. That is, even if the SBA legitimately grants or denies that business a loan for purely financial reasons, the SBA could be criticized from one quarter or another. Thus, it would appear that in order to avoid such criticism, the SBA simply excluded all businesses which could be involved, in any way, with opinion molding, whether or not any particular business might or might not actually disseminate controversial material.

If this is the rationale for the opinion molder policy, and we believe that it probably is, then, it may be a very neat bureaucratic solution to avoid controversy, but it would lack any legal

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justification. Size and financial condition are, in our view, the only relevant considerations for the SBA, not the avoidance of controversy or its own public relations.

While we question the legal basis for the opinion molder policy, even if, for the sake of argument, that policy can be justified, it is hard to see why motion picture theatres are included as ineligible businesses within the policy. In general, motion picture theatres are a part of the entertainment industry. The average motion picture theatre owner has as much relationship to the dissemination of particular political or philosophical viewpoints as a seller of television sets, or people who do typesetting. If general merchandise stores that also sell books, newspapers, magazines, records, etc. may be eligible for loans, then people who own theatres that show a general run of films for entertainment of the public, also ought to be eligible. There is no logical difference. A whole industry ought not to be deemed ineligible because, conceivably, there might be a theatre or two in some large city that possibly could be identified as showing strictly films with a particular political or philosophical point of view.

Neither should the industry be declared to be ineligible because there are so called "adult" theatres. The proposed rule change kept the exclusion of this type of theatre. If the SBA is justified in having an opinion molder policy, then it certainly would have the power to make this kind of distinction.

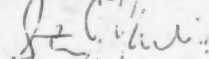
It is apparent that the SBA, itself, is very unsure of its position. According to the statement in the Federal Register of February 27, 1981, motion picture theatres were eligible for financial assistance from the SBA until 1978. Then several years went by during which theatres were not eligible. Then came the news of the rule change restoring eligibility and, finally, after months of inactivity, apparently another reversal of policy. Motion picture theatre owners want to be treated fairly, and this seesawing of the SBA is not fair treatment. Moreover, it is not the best of economic times for the motion picture industry, and so the policy of exclusion adds insult to injury.

The mandate of the SBA is to provide loans to small businesses. Whether or not the SBA decides to keep its opinion molder policy, it is neither logical nor fair to the motion picture theatre business to have it completely excluded from eligibility.

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We sincerely hope that you will go on with the enactment of the rule which would allow motion picture theatres again to become eligible for loans.

Sincerely,


Steven J. Riekes

SJR:sj

cc: Senator Edward Zorinsky
Senator James J. Exon
Senate Committee on Small Business
House Committee on Small Business
Congressman Hal Daub
Congressman David T. Dreier
Mr. John Dawsey, President
Theatre Equipment Association
✓ Mr. Robert Sunshine, Executive Director
Theatre Equipment Association
Mr. Joseph Alterman, Executive Director
National Association of Theatre Owners
Peter M. Fishbein, Esq., Counsel
National Association of Theatre Owners



FEB 24 1982

Mr. Steven J. Riekes
Richards, Riekes, Brown & Zabin, P.C.
Attorneys at Law
300 Overland-Wolf Centre
6910 Pacific Street
Omaha, Nebraska 68106

Dear Mr. Riekes:

Your letter of February 10 to the Administrator has been referred to this office for response.

It has been the policy of this Agency since its inception, as it was the policy of its predecessor agency, the Reconstruction Finance Corporation, not to make Government business loans to "opinion molders." This policy has been reaffirmed by every Small Business Administration Administrator. It has had periodic reviews by the Small Business Committees of Congress. In its report dated February 24, 1976, the Subcommittee on SBA Oversight and Minority Enterprise of the House Committee on Small Business reviewed and affirmed this policy but requested the issuance of clarifying regulations (House Report No. 94-840, 94th Cong., 2nd Sess., pp. 24-28). The revised regulations were issued in final form on December 21, 1976, 41 F.R. 55508.

Part of the basis for the proposed regulation change dated February 27, 1981 was that the "general audience" concept, similar to the existing "general bookstore" rule, constituted the only basis for an exception to the opinion molder rule for motion picture theaters. However, SBA believed that there was merit in the comments received that the proposed regulation change was not justified because of the arbitrary exclusion of some theaters. Therefore, upon further consideration, it was determined that no change will be made in our present policy which prohibits the making of loans to all theaters.

We appreciate your comments concerning this matter.

Sincerely,

A handwritten signature in cursive script that reads "Charles R. Hertzberg".

Charles R. Hertzberg
Acting Deputy Associate Administrator
for Financial Assistance

LAW OFFICES

Richards, Rickes, Brown & Zabin, P.C.

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Omaha, Nebraska 68106

March 15, 1982

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AREA CODE 402

OUR FILE NUMBER

87070-40-81

Charles R. Hertzberg
Acting Deputy Associate Administrator
for Financial Assistance
Small Business Administration
Washington, D.C. 20416

Dear Mr. Hertzberg:

I appreciate your taking the time to respond to my letter of February 10, 1982, in regard to the ineligibility of motion picture theaters for SBA assistance. Unfortunately, however, as a citizen, I am most disturbed by the language of your response. To be frank about it, your letter is vintage bureaucratese.

Movie theaters are denied eligibility because of the SBA's "opinion molder" policy. However, as raised in my letter of February 10, 1982, the issue is: By what statutory authority is the SBA justified in its formulation of this policy? The SBA, as an administrative agency, must perform its tasks strictly in accordance with the authority given to it by statute, and if there is no statutory authority, it cannot act. Your letter cites no statutory authority for this policy.

Instead, you attempt to justify the policy by saying that it has been a policy of the agency since its inception, and has been reaffirmed by every SBA administrator. The mere fact that an administrative body has operated under an erroneous or illegal policy for many years, does not make it less erroneous or less illegal. The passage of time, alone, cannot cure an unjustifiable position.

Your only other point on the opinion molder policy is to state that the Subcommittee on SBA Oversight and Minority Enterprise of the House Committee on Small Business, on January 24, 1976, "reviewed and affirmed this policy but requested the issuance of clarifying regulations (House Report No. 94-840, 94th Cong. 2nd Sess., pp. 24-28)."

I have read this report and I find no affirmation of this policy, whatsoever. In its report, the Committee noted that there have been "purported First Amendment" matters, but what was "purported" was

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never fully explained by the SBA, nor was there any detailed legal analysis. Instead, the SBA indicated that it did not want to be a censor of ideas, as that might violate the First Amendment. But, nowhere did the SBA explain why it would have to be a censor if it gave assistance to opinion molders. Consequently, the conclusion of the Subcommittee was as follows:

"The Subcommittee does not believe that the SBA should engage in activities which would necessitate its assumption of a censorship role. By censorship we mean the ability of SBA to direct a business as to what it can do or cannot do, relative to First Amendment protected activity, coupled with the power to enforce its will through use of sanctions. The Subcommittee believes such censorship would exist if SBA were to place in its loan agreements a prohibition against the promulgation of certain ideas and values, a breach of which would allow the Agency to liquidate the loan."

That statement is hardly an affirmation of the opinion molder policy.

Because the SBA might assist opinion molders does not mean that it would necessarily have to be a censor. The statute contemplates that the SBA will either grant or deny financial assistance based upon financial considerations. Such an operation has nothing whatsoever to do with censorship. As stated in my previous letter, the SBA apparently is afraid not of violating the Constitution by being a censor, but of the accusation of being a censor. And, the logic of avoiding the whole matter by refusing to make opinion molders eligible has much more to do with public relations than it has to do with the Constitution.

The illogic of this policy is revealed by the fact that current regulations allow operators of commercial broadcasting, radio and television stations, and cable television systems under the regulatory jurisdiction of the Federal Communications Commission, to be eligible for financial assistance. Certainly, radio and television stations are molders of public opinion. How is it that they are eligible and movie theaters, publishers, etc. are not? The typical SBA answer here is that those companies are regulated by the FCC. However, that is no answer at all. If we are really dealing with First Amendment problems, then those problems should exist whether those stations are regulated by another government agency or not. The First Amendment to the Constitution does not distinguish between the FCC and the SBA.

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The answer, of course, is that there would be no First Amendment problems at all, provided the SBA stuck to its statutory authority and either granted or denied loans solely on the basis of size and financial condition.

As I pointed out in my previous letter, even if it was possible to justify the opinion molder policy, it is most difficult to conceive a general movie house as an opinion molder. Consequently, I suggested that if you are not prepared to abandon the opinion molder policy, then, at least, you ought to enact the proposed rule change and allow movie theaters to be eligible as an exception to the policy. To this point you replied as follows:

" . . . SBA believed that there was merit in the comments received that the proposed regulation change was not justified because of the arbitrary exclusion of some theaters."

According to the proposed regulation, the only theaters that would be excluded are those showing strictly films with a particular political or philosophical point of view and so-called "adult" theaters.

As a practical matter, I am not certain whether there are any theaters that exhibit films strictly with a particular political or philosophical point of view. I simply cannot imagine that your policy of excluding an entire industry from eligibility would be dependent on the possible existence of what could not amount to, at best, more than an insignificant percentage of the total number of theaters.

The real nub of the matter is probably the exclusion of so-called "adult" type theaters. Again, as a practical matter, it may be questioned whether this type of theater would seek federal financial assistance or, even if so, whether the financial considerations involved might usually be too risky to justify SBA assistance. But, regardless, the existence of this type of theater should not be an excuse to exclude, wholesale, the movie theater industry.

It seems to me that it doesn't make any difference whether these types of theaters would be excluded or not. Why would their exclusion be any more arbitrary than the entire opinion molder policy already is? Furthermore, under current regulations, while general bookstores are eligible for SBA assistance, specialty stores primarily selling products that promote ideological, political or philosophical viewpoints are not. Consequently, if the SBA feels

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that it can make those kind of distinctions, then certainly it can make distinctions between these type theaters and general movie houses.

Let us assume, however, that in enacting the proposed regulations, adult type theaters were not to be excluded. What really is the problem in such an event? The only type of problem I can foresee is possible embarrassment by the SBA should it be criticized for rendering assistance to such an establishment. But so what? A government agency is not in business to avoid embarrassment, but to perform its function as set forth by law. The SBA would always have an answer for such a situation, namely, if Congress wished to exclude adult type theaters from eligibility, then the law should say so.

Until Congress specifically directs otherwise, the SBA ought to treat all small businesses with equality. It is Congress that defines the public interest, and not the SBA.

In any event, it is both unfair and irrational for all movie theaters to be excluded from eligibility because of concern about political movie houses if, indeed, there are any, or, so-called adult theaters.

In my judgment, there is still a right and a wrong, and no amount of bureaucratic gloss can obscure the issue. Either drop the opinion molder policy or enact the proposed regulation, and, in all events, do not exclude, arbitrarily, a whole industry composed of decent, honest businessmen who are performing a legitimate function in our economic system and for the American public.

Very truly yours,

Steven J. Rickes
Steven J. Rickes

SJR:sj

cc: Senator Edward Zorinsky
Senator J. James Exon
Senate Committee on Small Business
House Committee on Small Business
Congressman Parren J. Mitchell
Congressman Hal Daub
Congressman David T. Dreier
Mr. John Dawsey, President
Theatre Equipment Association
Mr. Robert Sunshine, Executive Director
Theatre Equipment Association
Mr. Joseph Alterman, Executive Director
National Association of Theatre Owners
Peter M. Fishbein, Esq., Counsel
National Association of Theatre Owners



APR 1 1982

Mr. Steven J. Riekes
Richards, Riekes, Brown & Zabin, P.C.
Attorneys at Law
300 Overland-Wolf Centre
6910 Pacific Street
Omaha, Nebraska 68106

Dear Mr. Riekes:

This will acknowledge receipt of your letter of March 15, 1982, setting forth your disagreement with the Small Business Administration "opinion molder" policy, and further questioning the Agency's statutory authority to impose such a policy.

The "opinion molder" policy was established by the SBA Loan Policy Board at the inception of the Agency, continuing the same policy established by its predecessor, the Reconstruction Finance Corporation.

The Loan Policy Board was created by P.L. 85-536 and now appears at Section 4(d) of the Small Business Act; which states in part:

"The Loan Policy Board shall establish general policies (particularly with reference to the public interest involved in the granting and denial of applications for financial assistance by the Administration and with reference to the coordination of the functions of the Administration with other activities and policies of the Government), which shall govern the granting and denial of applications for financial assistance by the Administration."

The SBA Loan Policy Board was abolished by Reorganization Plan No. 4 of 1965 (effective July 27, 1965; 30 F.R. 9353) and its functions transferred to the SBA Administrator.

Further, Section 5(b)(6) of the Act states:

"In the performance of, and with respect to, the functions, powers, and duties vested in him by this Act the Administrator may...make such rules and regulations as he deems necessary to carry out the authority vested in him by or pursuant to this Act..."

We believe the above information clarifies the question of statutory authority. As for the policy itself, our letter of February 24 sets forth the Agency views on the matter.

Yours truly,

A handwritten signature in dark ink, reading "Charles R. Hertzberg". The signature is written in a cursive, slightly stylized script.

Charles R. Hertzberg
Acting Deputy Associate Administrator
for Financial Assistance

LAW OFFICES

Richards, Rickes, Brown & Zabin, P. C.

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April 20, 1982

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TELEPHONE 558-1112
AREA CODE 402OUR FILE NUMBER
87070-40-81

Charles R. Hertzberg
Acting Deputy Associate Administrator
for Financial Assistance
Small Business Administration
Washington, D.C. 20416

Dear Mr. Hertzberg:

Your letter to me of April 1, 1982, is a woefully inadequate response to my letter to you of March 15, 1982.

I asked you to justify and support the SBA's so-called "opinion molder" policy, and, particularly, its exclusion of general movie theaters from eligibility. In my judgment, you have been unable to accomplish this task.

The first point you make in your letter of April 1, is to state that the policy has been around for a long time. However, as I stated earlier, "The mere fact that an administrative body has operated under an erroneous or illegal policy for many years, does not make it less erroneous or less illegal. The passage of time, alone, cannot cure an unjustified position."

Your second, and only other point, is to quote Section 5(b)(6) of the Act which gives the Administrator authority to "... make such rules and regulations as he deemes necessary to carry out the authority vested in him by or pursuant to this Act. . .".

The mere fact that an administrative body has the right to make rules and regulations does not justify any rule or regulation that that body may choose to make. One doesn't need to go to law school to know that an administrative body cannot do whatever it pleases. The Administrator cannot decree that everybody eat blueberry pie on Tuesdays. It is elementary that rules and regulations must be consistent with the Act.

" Legislation may not be enacted by an administrative agency under the guise of its exercise of the power to make rules and regulations by issuing a rule or

Charles R. Hertzberg
 April 20, 1982
 Page 2

regulation which is inconsistent or out of harmony with, or which alters, adds to, extends or enlarges, subverts, or impairs, limits or restricts the act being administered.

. . . It is the statute, not the agency, which directs what shall be done. A statute is not a mere outline of policy which the agency is at liberty to disregard or put into effect according to its own ideas of the public welfare." 1 Am.Jur.2d Administrative Law §132 at pp. 944 to 945.

In neither of your letters have you been able to state why the opinion molder policy is "necessary" in order to fulfill the intent of Congress. We can assume, then, that since the SBA has been unable to respond with anything more than bureaucratese, it cannot, indeed, justify its opinion molder policy or its exclusion of movie theaters from eligibility.

Mr. Hertzberg, I will concede that the opinion molder policy is not one of the great issues of our time. However, it does highlight the perils of bureaucracy, which is an important issue, causing anger and frustration among our citizens. In this case, a small but important number of small business people are being unjustly denied the benefit of a government program created especially for such people. This policy is another classical example of that unfortunate truth: that a bureaucratic institution regards as its first and paramount duty, its own preservation.

Given SBA's apparent unwillingness to thoughtfully re-examine the situation, as of the date hereof, I cannot state what avenues our client and others may choose to take to remedy this situation. However, because unrestrained bureaucracy is intolerable in a free society, I am confident that appropriate action of some kind will be forthcoming.

Very truly yours,

Steven J. Riekes

SJR:sj

cc: Senator Edward Zorinsky
 Senator J. James Exon
 Senate Committee on Small Business

Charles R. Hertzberg
April 20, 1982
Page 3

House Committee on Small Business
Congressman Parren J. Mitchell
Congressman Hal Daub
Congressman David T. Dreier
Mr. John Dawsey, President
Theatre Equipment Association
Mr. Robert Sunshine, Executive Director
Theatre Equipment Association
Mr. Joseph Alterman, Executive Director
National Association of Theatre Owners
Peter M. Fishbein, Esq., Counsel
National Association of Theatre Owners

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AREA CODE 402

OUR FILE NUMBER

87070-40-81

September 17, 1982

Robert Webber, Esq.
General Counsel
Small Business Administration
Washington, D. C. 20416

Dear Mr. Webber:

We are attorneys for Theatre Equipment Association, Inc., a national trade association of the theatre equipment industry.

Our client and others strongly object to the SBA's "opinion molder" policy, and, in particular, to the exclusion of motion picture theatres from SBA assistance under that policy. This past spring, we engaged in an extensive, but apparently fruitless, exchange of correspondence on this issue with Mr. Charles R. Hertzberg, Deputy Associate Administrator for Financial Assistance. A copy of that correspondence is enclosed.

Despite Mr. Hertzberg's cold shoulder, many in the industry have continued to attempt to change SBA's position. Undoubtedly, they were also encouraged recently because of the article in the Wall Street Journal of July 12, 1982, wherein it was reported that some SBA officials themselves conceded that the rule was "silly", and that the SBA ought "... to junk the opinion - molder rule...".

In regard to the foregoing, Mr. John F. Dawsey, Vice-President of Massey Seating Company, of Nashville, Tennessee, wrote to the SBA and received a reply from Mr. Hertzberg dated August 18, 1982. As Mr. Dawsey's firm is a member and he is the President of our Trade Association, he shared this correspondence with us, and a copy of the same is also enclosed.

As you will note, Mr. Hertzberg now attempts to justify the SBA's position based upon the Constitution and, presumably, the

COPY

Robert Webber, Esq.
 Dated September 17, 1982
 Page two

First Amendment. Mr. Hertzberg claims that the SBA has determined that it would not be in the public interest to "...include pornographic motion picture theatres and book stores, and those that deal in political, racial and pornographic greeting cards." However, he goes on to say, "...were the agency to attempt to make individual decisions on what is, or is not, in the public interest based on content, it would place itself squarely in a censorship position, which would also not be in the public interest, and which would be unconstitutional." Having raised this hypothetical dilemma, then, Mr. Hertzberg announces the SBA "solution" which is that the SBA "...had no choice but to maintain its position that all theatres were ineligible for assistance."

We believe, however, that Mr. Hertzberg's arguments are all flash and no fire.

There is no statutory mandate to exclude any kind of business, except a business which is not "small". If Congress has not required the SBA to exclude businesses that, in one way or another, might deal with political, ideological, or pornographic matters, why should the SBA presume to do so? We can find no statutory basis for SBA's position. We refuse to believe that the power to make rules and regulations is so broad that the SBA can arbitrarily exclude many categories of American business simply to avoid a hypothetical problem and a chimera of constitutional conflict.

It could be argued, just as well, that it is certainly not in the public interest to exclude, wholesale, an entire industry because a few theatres might show pornographic films.

Next, the SBA's own rules and regulations betray it's position. They provide that "general book or music (record) stores" are eligible for SBA assistance. What is the definition of a general book store? Many, if not most book stores, sell religious, political, ideological, and frequently pornographic material. So, whatever the definition may be of a general book store, I should think it impossible to determine when a general book store ceases to become one, unless you also make a judgment as to the "content" of the material which it sells.

Robert Webber, Esq.
 Dated September 17, 1982
 Page three

We see little difference between a general book store and a general movie theatre. However, when confronted with this question, the SBA, has been desperate to find a response. We understand that the SBA wrote a letter this summer to Senator Jennings Randolph suggesting that "at any given time", a general book store "passively presents a wide range of topics and titles", whereas, a movie theatre would selectively present an individual work. Why is a moment in time relevant at all, vis-a-vis this issue? If it is, suppose a general book store decides to go on a campaign to push the Bible, a book about Ronald Reagan, or a special on Penthouse magazine? Or, on the other hand, suppose there is a movie theatre which shows six or eight or more films simultaneously? Can there not be moments in time when a general book store ceases to be "general", or when a movie theatre can be said to present a wide range of subject matter?

The SBA's position is contradicted by another example: radio and television stations and cable TV systems are eligible for assistance. Indeed, the regulations provide that "...no consideration will be given to the applicants present or proposed program schedule, or to the content of any particular program; but SBA reserves the right to exercise all the rights and remedies afforded a creditor under the laws of the United States..."

There is absolutely no logical difference between a movie theatre and a broadcasting station, including the specious distinction of time. We understand the SBA's response here is that broadcasting stations are regulated by the Federal Communications Commission. However, what difference does that make in any constitutional sense? The First Amendment makes no distinction between one federal agency and another. If it is unconstitutional for the SBA to get involved in these matters, then it is equally unconstitutional for the FCC to do so. If this constitutional argument had any merit at all, then would it not be unethical for the SBA merely to respond by passing the constitutional buck to the FCC?

Perhaps the most significant exposition of the weakness of SBA's present position are prior opinions of your own office. Prior to 1978, on at least two occasions, 81 O.D. 155(1971) and

Rqbert Webber, Esq.
 Dated September 17, 1982
 Page four

92 O.D. 103 (1974), opinions of your office indicated that movie theatres were eligible for loans. Indeed, it wasn't until 1978, in an opinion, 111 O.D. 104, that it was held that movie theatres were not eligible. And then, shortly after that opinion, in 117 O.D. 102, issued in 1980, the General Counsel of SBA, in very strong language, indicated that the 1978 opinion was disavowed and should not be followed. I quote from that opinion:

"This opinion necessarily overrules the opinion discussed at 111 O.D. 104, p. 1461 (1978), holding motion picture theatres ineligible for SBA assistance. The 1978 opinion failed to address the precedent in 92 O.D. supra; ignored an analogous precedent at 81 O.D. 155, p. 953 (1971), holding that producers but not exhibitors of motion pictures were ineligible for SBA assistance; and was based on an extremely broad and literal interpretation of the opinion molder rule which is now being expressly disavowed."

Considering the foreceful language of this opinion, issued only two years ago, it would appear that SBA's current position, that movie theatres are ineligible, is without valid support.

In view of the prior opinions of your office, and, considering the fact that neither the law nor the regulations have changed on this issue, it is very odd indeed that the SBA would now issue a different interpretation and exclude motion picture theatres from eligibility. The peculiar nature of SBA's current position is compounded considering that it comes under an administration which has promised not only to aid small businesses but also to end bureaucratic excesses. Certainly this is a classic example of bureaucracy, in the pejorative sense, at work.

In light of the foregoing, it seems to me there are three possible choices available to the SBA, any one of which would be basically acceptable to our client's industry:

1. The SBA could throw out the opinion molder policy altogether. This would be in keeping with statutory language, and would open SBA's doors to many categories of American businesses that appear to have been arbitrarily excluded from assistance.

Robert Webber, Esq.
Dated September 17, 1982
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Not only that, but it would be a most cost effective measure. Consider the numerous man hours that would be saved in not having to interpret the illogical labyrinth that this regulation provides.

2. The SBA could enact the regulation it proposed in February of 1981 specifically allowing movie theatres to become eligible, even under the opinion molder policy. This might exclude a few adult type theatres from assistance, but so what? If, for the sake of argument, SBA has the power to have issued the opinion molder regulations to begin with, including the provisions regarding a general book store, then, it would also have the power to make this exclusion. And, if by some remote chance, some x-rated movie house were to take the SBA to court on this issue, certainly that would not be the worst thing to have ever happened to the SBA. At least, this way, an entire industry would not be denied fair treatment because a few on the outer fringe of that industry might, hypothetically, make some complaint.

3. Your office could simply revise the current interpretation of the policy and go back to the position of your office in 1980 allowing motion picture theatres to have eligibility. Indeed, I should think that your office would be rather embarrassed in trying to defend SBA's current position, particularly considering SBA's own record on this matter.

The motion picture industry, and in particular, the owners of motion picture theatres, deserve better treatment than the SBA has meted out to them recently. We trust that you will thoughtfully consider the foregoing and take immediate action to help resolve this matter.

Very truly yours,

STEVEN J. RIEKES

SJR/bls

Enclosures

Robert Webber, Esq.
Dated September 17, 1982
Page six

cc: James C. Sanders
Charles R. Hertzberg
Members Senate Committee on Small Business
Members of the House Committee on Small Business
John Dawsey
Robert H. Sunshine
Joseph Alterman
Peter M. Fishbein
Jerome Gordon
Various Other Members of the House and Senate

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MONDAY, JULY 12, 1982

THE WALL STREET JOURNAL.

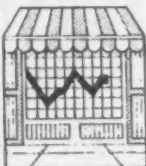
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SMALL BUSINESS

Movie Loans . . . Getting Break On Taxes . . . Minority Cut-Off

IF THE SBA SAYS a movie is "intellectual property," what does it call one like "The Texas Chain Saw Massacre"? The Small Business Administration won't help movie theaters because of a rule that prohibits help for a business "engaged in the creation, origination, expression, dissemination, propagation or distribution of ideas, values, thoughts, opinions or similar intellectual property, regardless of medium, form or content."

The idea is to keep the government from interfering with "opinion molders," the SBA says. A lofty goal but it's one the agency reaches for with one hand while another dishes out exceptions. For example, cable-TV operators, who have been known to distribute "intellectual property" in the guise of movies, can qualify for SBA financing. The rule is silly, some SBA officials concede. Last year, the agency published proposed changes that would permit loans to movie houses—except those showing "sexually oriented" films or outright propaganda movies.



The proposal was withdrawn, and nothing has been done since to help movie houses. The proposal was dropped because excluding porno houses would have been unfair, the SBA says. A better remedy, SBA staffers say, would be to junk the opinion-molder rule, and adopt one saying that any legal small business is eligible for aid.



U.S. GOVERNMENT
SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

OCT - 7 1982

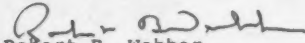
Mr. Steven J. Riekes
Attorney at Law
Richards, Riekes, Brown & Zabin, P.C.
6910 Pacific Street
Omaha, Nebraska 68106

Dear Mr. Riekes:

This refers to your letter of September 17, 1982, with enclosures, concerning the policy of the Small Business Administration of not providing financial assistance to motion picture theaters. The Deputy Associate Administrator for Financial Assistance, Charles R. Hertzberg, has corresponded with you and Mr. Dawsey and has presented, in detail, the Agency position. His letters of February 24, April 1, and August 18, 1982, set forth the background and the rationale for this policy. We can add nothing to his explanation.

Each successive Administrator of SBA has supported this policy pursuant to his authority under Sec. 4(d) of the Small Business Act, as amended by Reorganization Plan No. 4 (30 F.R. 9353), which supplements the rulemaking authority under Sec. 5(b)(6) of the Act. There is no plan to change this position.

Sincerely,


Robert B. Webber
General Counsel

102 Business Loans and Development Company Loans—Eligibility of Theater
/Entertainment Center

Our opinion was requested on the eligibility of a small business concern for SBA assistance in the form of both a Section 502 loan guarantee and a companion Section 7(a) loan guarantee. The proceeds of the loans would be used to construct an "entertainment center," which would include a theater (featuring musical entertainment only), restaurant, disco and lounge.

The precise question presented is whether 13 C.F.R. § 120.2(d)(4)—the so-called "opinion molder" rule—bars such assistance. The rule does not prohibit SBA from guaranteeing the loans. This conclusion is based on past interpretations of the rule, the underlying purpose of the 1976 amendment of the rule, and the language of the rule as amended.

Prior to the extensive 1976 amendment of the rule, an applicant would have been able to receive SBA assistance. In 92 O.D. 103, p. 1109 (1974), this office approved a Section 502 loan under circumstances similar to those involving applicant. We based our

conclusion that the small business was eligible for SBA assistance on the fact that the concern itself would not create or present the plays or other forms of entertainment; the concern would merely hire or "book" entertainers who would perform those functions. We reiterate an earlier opinion to the effect that an applicant "who provides premises, an auditorium, or a theater for live bands or orchestra, and collects admission charges, is eligible for SBA financial assistance." 83 O.D. 101, p. 984 (1971).

In light of this clear showing that applicant would have been eligible for assistance under the old version of the opinion molder rule, it is well to consider whether the 1976 amendment of the rule was intended to restrict eligibility further and perhaps overrule these precedents. There is no indication, nor even the slightest suggestion, that the rule was amended for that purpose. Rather, the rule was rewritten in more specific terms in an attempt to clarify its dimensions—not tighten its restrictions. See 41 F.R. 23731 (June 11, 1976) and 41 F.R. 55508 (December 21, 1976). The amendment followed hearings evidencing Congressional discomfort with the vagueness of rule as then written and the expansive as well as inconsistent manner in which SBA had implemented it. See H.R. Rep. No. 94-840, 94th Cong., 2d Sess., at 24-28 (1976).

It would thus be ironic if SBA were to interpret the amended rule inconsistently with precedent, in such a way that a small business which clearly would have been eligible for assistance prior to the amendment, is now deemed ineligible. Accordingly, unless the language of the present rule compels that result, the rule should be interpreted in a manner consistent with both its underlying purpose and the underlying purpose of the Small Business Act.

The amended rule states that "producers, importers, exporters or distributors of communications, including...theatrical productions" are ineligible for SBA assistance. 13 C.F.R. § 120.2(d)(4)(ii). While this language could be very broadly interpreted to equate the booking of musical entertainment by a theater with the "dissemination...or distribution...of ideas," that is not the only nor the most reasonable interpretation of the rule. In light of the history and purpose of the rule, this office declines to construe its terms in such a broad fashion. Accordingly, whatever the scope of the "distribution of ideas" concept, an applicant which plans to use SBA assistance to construct an entertainment center is not prohibited by the opinion molder rule from receiving such assistance.

This opinion necessarily overrules the opinion discussed at 111 O.D. 104, p. 1461 (1978), holding motion picture theaters ineligible for SBA assistance. The 1978 opinion failed to address the precedent in 92 O.D. *supra*; ignored an analogous precedent at 81 O.D. 155, p. 953 (1971), holding that producers but not exhibitors of motion pictures were ineligible for SBA assistance; and was based on an extremely broad and literal interpretation of the opinion molder rule which is now being expressly disavowed. [Agency policy on theatrical ventures is currently under review.]

Mr. STENHOLM. Thank you, Mr. Riekes.

Mr. RIEKES. Thank you.

Mr. STENHOLM. You have used the word "legitimate" small business many times in your testimony, in both your written and also in your verbalizing your statement. Would you give us your definition of a legitimate small business?

Mr. RIEKES. I think legitimate means legal, not some business that is illegal. It depends on the jurisdiction. In some places gambling is illegal. Well, then, I don't think in that jurisdiction SBA should be loaning money to a business that is going to be operating illegally.

Other than that, it depends on the jurisdiction and it depends on which laws you're talking about and it depends on which business. Basically a legitimate business is a legal business.

Mr. STENHOLM. Do you believe that SBA should make a loan to a pornographic cookie company?

Mr. RIEKES. I am not advocating that they make loans to pornographic cookie companies, but I think that generally baking is a legitimate business. If baking pornographic cookies is not illegal, then I'm willing to accept the risk that maybe somebody is going to come along with some weirdo cookies, rather than taking the approach of saying "hey, all bakers should be thrown out the window because that might happen."

Mr. STENHOLM. There have been numerous Supreme Court decisions covering the constitutional ability to regulate the area of idea communication, which you have talked about. Do you know of any decisions covering the Government's ability to put such a business into existence or to put it out of business?

Mr. RIEKES. I cannot recall right now specific Supreme Court decisions on that issue. But for instance the FCC may take away a license and put someone out of business. There are constitutional questions about prior restraint of newspapers by State laws. Those have usually been ruled unconstitutional. But right off the top of my head, I cannot quote any case or give you any citation, no.

Mr. STENHOLM. What if SBA were to grant a loan and a year or two later the business starts promoting political or religious ideas, what do we do then?

Mr. RIEKES. Well, I think you can have certain conditions in the loan that you can insert. One is that the borrowers still operate legally within the terms of the law, that means not only Federal law but it means State and local laws. I think, two, that they have to follow the purposes for which they got the loan, basically, and I think those are legitimate criteria, too. I think that is the best the SBA can expect as conditions for granting the loan, and if they violate those conditions, then a default can be declared.

Mr. RICHARDS. Mr. Chairman, may I add a comment?

Mr. STENHOLM. Surely.

Mr. RICHARDS. I don't see, with reference to movie theaters or publications of any type, that that situation is any different than the situation that the SBA faces today. It can make a loan, for instance, to a restaurant or a retail department store which 6 months from now may put up some signs or placards, or distribute bulletins or brochures in its business, advocating a political philosophy or a religious philosophy, or it may distribute pornographic

material within the restaurant or within the department store. Whatever the SBA's policy is today in that regard should be no different, as far as I can see, whether it is that type of a business or whether it's a movie or a magazine.

Mr. STENHOLM. Thank you. That's a very good point.

I will defer further questioning now to Mr. Roth.

Mr. ROTH. Thank you, Mr. Chairman.

I appreciate your testimony and also appreciate your opinion. I think that your arguments are very good, very good legalistic arguments, but I don't know how good they are in the arena of public opinion.

If we use this legal business doctrine, a loan could be made to a house of prostitution in Nevada, for example, where it is legal. I don't know how well that would sit with my constituents back in Wisconsin, using Government funds to promote something like that.

Mr. RIEKES. In the present regulations, Congressman, to my knowledge, nothing would prohibit the SBA right now from giving a loan to a house of prostitution in Nevada. They don't have any policy on that, as far as I know. The best that they could say is that's kind of a borderline business and maybe there's a chance that the law will change, or there are other problems with it, and therefore it's not creditworthy.

Mr. ROTH. The opinion molder rule I think is one that SBA is concerned about because SBA is subject to a great deal of public opinion, as all our agencies are, as we are in Government. When making laws in the political arena you have to look at public opinion and not only at the legalistic arguments.

Mr. RIEKES. That is correct. But you have heard testimony from organizations representing tens of thousands of people, people who America accepts as part of its national economy. Jobs are dependent on them. Are we going to say that all of these people are frozen out because maybe somebody in the future might apply who we don't like? Does that balance very well? What about public opinion there?

Mr. ROTH. First of all, I don't know if I would go to that extreme. There is possibly a problem with interpretation of the opinion molder rule. Maybe it is too broad, but just to do away with it totally, I think we're probably going too far in the other direction. To do away with the rule totally I think is something that Congress is going to have to give some thought to. Because if we do away with it, it's going to be a lead pipe cinch that we're going to have some problems in this area.

Now, as I say, the opinion molder rule might be too broad. I can see an argument for reform, but to do away with it completely I think would be going too far in the other direction.

Mr. RIEKES. Well, we're not advocating that it be abolished completely, in the sense that we have put into our bill several limitations—one, advancing or inhibiting religion; two, advocating the overthrow of the Government; and three, as I said, the question of the legality or possible illegality of the business.

This is something that deserves further study: Congressman Adabbo's bill contains, in lines 10 and 11 that assistance would also be denied if it was adverse or detrimental to legitimate public in-

terest. I think that may be worthy of further study and that language may address the problem that you're talking about, conceivably.

Mr. ROTH. Thank you very much.

Mr. RICHARDS. Mr. Roth, may I elaborate briefly on the point that was just discussed?

We, of course, are primarily interested in the motion picture industry. We are here as counsel for the Motion Picture Theatre Equipment Association. The illustration that you cited concerning a possible loan to a house of prostitution as being unpopular, I think we ought to give that very thorough consideration, because that certainly is not governed by the opinion molder rule. As Mr. Riekes pointed out, that type of loan conceivably could be eligible under the current SBA policy. Yet, to our knowledge, that has never presented a problem to the SBA.

To our knowledge, prior to 1978, when motion picture theaters were eligible for SBA loans, there had never been a problem as far as applications from pornographic movie houses. For instance, at least the SBA has never cited that instance or that reason for changing its policy.

Now, as Mr. Riekes indicated, we are certainly agreeable to any kind of amendment to the bill, or any kind of regulation that might be necessary to protect the public interest. I think the Federal Communications Commission has power to license or take away the license of a radio or television station for advocating political philosophy or what have you. I think that in some manner, if it is necessary, if the committee or the Congress feels it is necessary to insert further exceptions into the law, or further limitations, we certainly would be agreeable to anything that you would deem appropriate in that regard.

Our primary interest is to the people whom you have heard testify thus far—and I understand there will be some other groups testify later—are primarily interested in the motion picture theater industry. To our knowledge, the problem of loans to pornographic movie theaters has never been a problem when theaters were eligible for loans, but if it is necessary or desirable to insert some limitation to cover that, we certainly are agreeable to it.

Mr. IRELAND [presiding]. Mr. Bilirakis, any questions?

Mr. BILIRAKIS. Mr. Chairman, I am pleased to hear both testimonies, particularly Mr. Richards' explanation. I personally would distinguish between the small theater owner, *The Daily Worker*, and a house of prostitution, if you will, and some newspapers that would espouse particular political philosophies and that sort of thing.

Mr. Riekes is an exceptionally good attorney and, as Mr. Roth says, he has very good legalistic arguments, but if I try to make those arguments to my conservative constituents on the west coast of Florida, God help me. So these are the things that we have got to be concerned with and those public policy arguments are very, very significant. We cannot belittle those in any way whatsoever.

Personally, I don't think even though I said at the outset we have got to be objective and hear the other side, I also at this stage don't see myself having too much trouble with the small theater owner portion of this. But when you get in here and give us argu-

ments on a broad plain and bringing all of these other areas, no, I don't think we should cut out loans to all cookie makers. But I think we have got to be concerned about even that one illegitimate, again, the definition of the word "legitimate" is worthy of a thousand and one different definitions.

Well, I thank you, Mr. Chairman.

Mr. RICHARDS. I might just add that, of course, Mr. Riekes' comments are being made to express his views, and once we have heard the objections that may be presented by the SBA or opponents at the subsequent hearing, of course, we would welcome—and I understand we will have an opportunity to respond to those. But I did want to make it clear that we are not blind to the concerns of the committee or the concerns of the Congress or the SBA, and certainly, from our standpoint, would recognize any appropriate exceptions that you may deem appropriate.

Mr. RIEKES. If I may, because there is a bifurcated hearing here, and because the SBA has ostensibly stood on what they say is a legal foundation, I had to lay out, Congressman, those legal issues. Now that we have identified the real problem, I am saying I am sensitive to those issues. But let's deal with it on that plain. But, we don't have to be so draconian in our approach to solve the problem that you talked about by throwing out whole classes and categories of businesses to solve that problem. At least I would hope that we would have the ingenuity not to have to go to that extreme. That was the only point.

Mr. BILIRAKIS. Thank you.

Mr. IRELAND. That is a disease that has infected the bureaucracy, however.

Gentlemen, we thank you very much. We appreciate your help. You did mention, and as I said at the outset and will reiterate again, the SBA and others on the other side of the fence will testify after the first of the year. Everyone here will have an opportunity to submit for the record their comments on that. It's the only fair way to do it.

Thank you very, very much.

Mr. RIEKES. Thank you, Mr. Chairman.

Mr. IRELAND. Our next witness is C. E. Scott from Scotsman Law Books, Inc., Austin, Tex. Mr. Scott, welcome.

TESTIMONY OF C. E. SCOTT, SCOTSMAN LAW BOOKS, INC.

Mr. SCOTT. Good morning, gentlemen.

I certainly appreciate the time and consideration you are giving H.R. 1157. We feel that the SBA regulations in their present context which arbitrarily deny a loan to any business engaged in the creation, origination, expression, dissemination, propagation, or distribution of ideas, values, thoughts, opinions, or similar intellectual property are discriminatory and create an unnecessary hardship on many small businesses.

We have noted that these regulations were written to prevent the Government from interfering with the media or the distribution of media products. It seems to us that denial of eligibility is an interference. We are singled out because we choose to retail a book

rather than some other product. Then, access to a Federal program, which is funded through our tax revenue, is denied.

The primary result of this regulation places an impediment in the path of some small businesses which other small businesses do not have to overcome. It is extremely disheartening to start a business, spend 12 years of your life to improve it, and then find in some ways you are less equal.

As we see it, a strict interpretation of the regulations now existing would deny a loan to any business. Advertising any product or service is an expression of an idea or thought. It is certainly an attempt to propagate an idea and influence the behavior of the public at large.

We notice that a firm engaged in printing will not be denied a loan under the present regulations because the printer has no direct financial interest in the commercial success of the material. See SBA title 13 (120.2(I)).

It would seem in this case that a direct interest in the success of the material is the determining criteria. We will submit that a bookstore alone that is engaged in the retail sale of material produced by numerous publishers has no direct interest in the success of a particular volume any more than a printer setting the type and printing the material. The bookstore is engaged in retailing a product in the expectation of earning a profit, just as any printer is selling a service for the same reason.

Scotsman Law Books, Inc., along with several other legal bookstores, restricts our inventory to legal materials such as you will find in any law office. We have single volumes and sets covering such areas as State statutes and codes, Federal statutes and codes, State and Federal reporters on cases, legal forms, legal encyclopedias and dictionaries, copies of the U.S. Constitution, copies of the Declaration of Independence, and various other legal materials.

Most of the legal bookstores are not engaged in publishing, and, so far as I am aware, in the few that are publishing materials, the publishing entity is operated as a separate business. At my company, as in most other bookstores, we are simply retailing a product created and produced by publishers with whom we have no financial interest in common. Specifically, we do not have any interest in their financial well-being or in a particular publisher's continuing existence. In short, we retail a product which in this instance happens to be a book and/or a set of books. We have no interest in what item is selling, but only that items are sold so as to produce revenue and a profit, if possible.

We think the regulations should be amended so that the determination of eligibility should depend on the ability to make repayment, or the regulations be amended to apply the same criteria to all business enterprises.

This is off the record, Mr. Ireland. I simply think that the regulation, as it exists, is written way too broadly. I would like to see it narrowed down where certainly we wouldn't be in the position of funding a Nazi bookstore, communistic ideas, the Daily Worker, or, as in previous testimony, questionable enterprises. But I can safely say, although I don't know all the jurisdictions you people represent, that my company does sell to people in your jurisdiction because we sell all over the United States. We sell only to lawyers.

We deal only in working legal materials. We have no connection and, frankly, most of the publishers would like to see us out of business because we're paying more for the product than they would pay themselves if they have to buy it back.

We could manipulate a little bit and qualify as a general bookstore, but I simply feel the regulation applying to legal bookstores is wrong. That's my statement, sir.

Mr. IRELAND. Mr. Scott, please explain to me, because I'm not sure I totally followed your last statement there. Who did you say it was that would like to see you out of business?

Mr. SCOTT. Publishers of the material we handle. Specifically, let us say, the West Publishing Co. They are the largest, by far, I believe, in the legal publishing industry. They sell everything and they almost have a monopoly on it. They will pay, for instance, 75 cents a book if they buy it back, whereas we might pay anywhere from \$5 to \$12 a volume, and then resale it for \$14 to \$15.

Mr. IRELAND. You can tell I'm not a lawyer and am not all that familiar what goes on in that outfit.

Mr. SCOTT. Our industry is similar to your college bookstore when you were attending college. If you recall, you bought your books, and then at the end of the semester you took them back. We do the same thing, except for attorneys.

Mr. IRELAND. We have a gentleman farmer. I'll ask him next. Mr. Stenholm.

Mr. STENHOLM. I believe you just answered the one question I was going to ask you. We might reiterate it.

In your last paragraph in your statement you say, "We think the regulations should be amended so that the determination of eligibility should depend on the ability to make repayment, or the regulations be amended to apply the same criteria to all business enterprises."

My question was, which of the two was your preference?

Mr. SCOTT. Well, before I arrived here I hadn't really considered that the SBA would be funding pornographic movies or bookstores or this type of enterprise. I frankly had never thought about that.

I meant in the sense of all legitimate businesses, and I will use the same definition. A legitimate business to my mind is one that you could go home and tell your constituents about without getting voted out of office. [Laughter.]

Mr. STENHOLM. I think I understand that definition very well. I don't think I can add to that one.

Mr. IRELAND. You're going to quit while you're ahead.

I was afraid we were going to say the SBA loans were the loans of last resort and those kind don't need them; that's what worries me.

Mr. BILIRAKIS. Mr. Chairman, I like his definition a little better than I like Mr. Riekes'. It's more practical and realistic, but it certainly is not more legalistic or more constitutional.

Mr. SCOTT. We do have to recognize that we live in the real world.

Mr. BILIRAKIS. So your firm deals strictly with legal periodicals? You said the West Publishing Co., Am. Jur., Corp. CJS, et cetera?

Mr. SCOTT. That's correct, sir. Just with legal periodicals. We deal with West, Bancroft, Callahan, Mickey, and Harrison. Who knows; there are several hundred legal publishers.

Mr. BILIRAKIS. And you have applied for a small business loan and been denied?

Mr. SCOTT. Yes, sir.

Mr. BILIRAKIS. You don't deal with any legal periodicals which are out of the ordinary? I don't know of any illustrations or examples of that.

Mr. SCOTT. No; we deal with American laws, Federal and State. We deal with statutes, cases, forms, et cetera, the type material you just mentioned strictly, and that's it.

Yes; we have applied for a loan and have been turned down.

Mr. BILIRAKIS. I would be interested in getting the SBA explanation as to why they would be denied SBA financial assistance.

Mr. IRELAND. I note that your attendance will be expected at the hearing after the first of the year.

Mr. BILIRAKIS. Thank you.

Mr. IRELAND. Mr. Stenholm, anything further?

Mr. STENHOLM. I was just going to add that as a farmer, a school-teacher, and a nonlawyer, I have the opinion that most legal instruments are out of the ordinary. [Laughter.]

But I don't think I would use that to deny an SBA loan.

Mr. BILIRAKIS. As a lawyer, I think I would even agree with that.

Mr. IRELAND. Thank you very much, Mr. Scott. We appreciate you coming to talk to us.

Mr. SCOTT. Thank you.

Mr. IRELAND. Our next witness is Mr. Gary Smith, executive vice president, Greeting Card Association, Washington, D.C. Welcome.

TESTIMONY OF GARY K. SMITH, EXECUTIVE VICE PRESIDENT, GREETING CARD ASSOCIATION

Mr. SMITH. Thank you, Mr. Chairman, and members of the subcommittee, for the opportunity to present our views on H.R. 1157.

I am Gary K. Smith, executive vice president of the Greeting Card Association. We are the trade association of the greeting card publishing industry. The member companies of our association annually produce approximately 75 percent of the estimated 7 billion greeting cards consumed in the United States. These products are distributed through a retail network of approximately 150,000 outlets throughout the 50 States.

Mr. Chairman, the issue before this subcommittee today is, very simply, whether the Small Business Administration should be permitted to continue its present policy of denying financial assistance to any business "engaged in the creation, organization, expression, dissemination, propagation or distribution of ideas, values, thoughts, opinions, or similar intellectual property, regardless of medium, form, or content."

In our view, the SBA should no longer be allowed to continue to refuse assistance to qualified small business concerns solely because their primary business activities are to communicate ideas or to mold opinions. We hold this view for many reasons.

Perhaps the most important reason is that application of this rule to a select group of small businessmen appears to have no constitutional or statutory grounds. Certainly there seems to be no substantiation either in the Constitution or in the Small Business Act itself for this rule. In fact, it seems more likely that by denying financial assistance to firms engaged in communication activities, the SBA has denied first amendment protections within the Constitution itself. First amendment rights cannot and should not be sacrificed merely because of a notion or fear that some evil may occur through the exchange of free and open ideas. Instead the Government, and specifically the SBA, should encourage the free flow of ideas.

Second, the primary role of the SBA is to provide financial assistance to small businesses that meet the SBA's financial criteria. The products or services offered by these businesses are or should be irrelevant if they appear to have economic viability and are legal under Federal and State law. Yet, SBA application of this rule arbitrarily ignores the fundamental issue of economic viability and in so doing apparently violates its own statutory goal.

Third, by refusing assistance to businesses in the communications industry, the SBA has been unable to promote small business activity in an increasingly vital element of contemporary society—the compelling need for more information and more ways to communicate that information. Denying financial assistance to small businesses who can bring innovation, creativity, and as importantly, price and service competition to this industry, at best seems socially and economically counterproductive.

Finally, we believe that the opinion molder rule as it exists creates arbitrary and occasionally illogical decisions when the rule is applied by the SBA. An immediate example is the greeting card industry. The SBA has rightly determined that greeting cards are communication products. By applying the opinion molder rule, small manufacturers of greeting cards are ineligible for SBA assistance. Yet greeting cards do not seek to communicate or impose ideas or opinions held by the manufacturers of those greeting cards on either the buyer or the recipient of our products. Rather, it is the product buyer who seeks to deliver a message to the card receiver. Most usually that message is one that deals with human emotions of love, compassion, concern, or joy.

Our industry is particularly marked by a persistent demand for creativity and choice by consumers. To deny assistance to small or emerging greeting card publishers that bring new or fresh ideas to the marketplace has a stifling effect on both product creativity and product choice for our consumers.

Mr. Chairman, the Greeting Card Association strongly supports the intention of H.R. 1157 and urges passage of it or similar legislation which will strike down the opinion molder rule.

Mr. IRELAND. Thank you very much, Mr. Smith.

Mr. Stenholm, any comments?

Mr. STENHOLM. Thank you, Mr. Smith, for your very good testimony. The one on greeting cards is a very good point.

I don't believe I have any questions, but the thought has just occurred to me that might be relevant to this testimony, to reflect on the Legal Services Corporation, which is a product of the Congress

of the United States. It's sole purpose in origination was a very noble one, one I think which most if not all Members of Congress would support, and that is to provide legal service for those unable to provide it for themselves. That institution of Government, though, got involved in the public opinion area and became a very strong public opinion molder, and in so doing began to incur the wrath of Members of Congress who felt that it should not be in that business, that it should be strictly in the business of providing legal services for those unable to provide it for themselves.

I think there is an analogy that could be drawn here, one in which a point has been made of all of those testifying this morning, and that is the broad brush is being used rather than zeroing in or using a rifle in recognizing differences within industries. I think that has been the concern expressed by many on this committee, that we don't necessarily want to get involved in areas that public opinion would not be on our side.

At the same time, the point you have made, and others before you have made, is that under the current interpretation of the regulation, legitimate businesses, as best defined by the previous witness are being denied assistance, and I think, Mr. Chairman, we should look at the Legal Services Corporation and the great controversy surrounding that organization and use that for a benchmark on which to build further with this legislation.

Mr. IRELAND. A good point.

Mr. Bilirakis.

Mr. BILIRAKIS. Mr. Smith, you would then be a proponent of completely deleting any opinion molder policy?

Mr. SMITH. I think that, at least in our opinion, the opinion molder rule, as it presently exists, allows the SBA to provide too much in the way of subjective judgment relative to whether or not they are serving the public interest, as well as their own statutory goal.

Mr. BILIRAKIS. You're not suggesting modifying that; you're suggesting just the broad brush that Congressman Stenholm referred to; you're suggesting that that broad brush be conversely used to wipe out the entire policy?

Mr. SMITH. I think at this point in time philosophically we would agree that the broad brush approach would work best, at least under present constitutional as well as statutory law, particularly as it relates to the SBA's principal goal, which is to assist small business in the arena of competition and product delivery.

I think, practically speaking, obviously we would look very closely at or be supportive of any amendment to the proposed legislation which would add to public interest as a goal of the SBA. My only concern philosophically again is that serving the public interest is largely in the eye of the beholder, and using Mr. Stenholm's example of Legal Services Corporation, when do they become that which does not serve the public interest or the interest of the Congress which created it. So, philosophically and practically, I think there are two separate issues to be very closely examined.

Mr. BILIRAKIS. Of course, the eye of the beholder as far as we're concerned is our eyes represent 500,000 to 600,000 people back home, so that is the eye of the beholder which we're concerned

with, and rightly so. After all, this is a republic and this is why we're up here.

Thank you, Mr. Chairman.

Mr. IRELAND. Thank you, Mr. Bilirakis.

Mr. Smith, thank you very much for your clear and concise testimony.

Mr. SMITH. Thank you.

Mr. IRELAND. Our last witness is David Godine, president of David R. Godine Publisher, Boston, Mass.

TESTIMONY OF DAVID R. GODINE, PRESIDENT, DAVID R. GODINE PUBLISHER, INC., ACCOMPANIED BY RICHARD SCHMIDT, LEGAL COUNSEL, AMERICAN ASSOCIATION OF PUBLISHERS

Mr. GODINE. Thank you, Mr. Chairman. I am here with counsel for the American Association of Publishers, Mr. Richard Schmidt. This is essentially the AAP's position with which I substantially agree as a small and independent publisher. I appear before you today on behalf of that association, which has 300 active members and represents 85 percent of all books published in America. I guess I am the only person at this hearing speaking for the book publishing industry, the book publishers rather than purveyors of books.

Our members range from the very small, single entrepreneur, the mom-and-pop operations, to family-sized companies, to larger closed corporations, sizable publicly traded companies, and very large communication conglomerates—something with which I am very personally concerned.

Until 1978, as we have heard numerable times, the SBA has consistently refused financial assistance to all enterprises involved in the dissemination of ideas and values. I learned this late in life when I went for a loan and was refused on this basis. This was a policy adopted without mandate from Congress, in the belief that SBA would thus avoid any appearance of governmental interference with freedom of expression.

But on January 27, 1978, SBA modified its policy and allowed loans to the electronic media, radio, and TV, but continued to exclude the print media—books, newspapers, magazines—without acknowledging, or I might add, explaining any basic inconsistency in that policy.

I would like to precise, if I could, because it seems to me that most of these questions have been raised and have been answered adequately. I don't think I should rehash them.

The number of book publishers in this country has increased in the past 10 years, as has the number of books published. I don't think this is an industry that lacks any diversity within itself. It's an active industry. It is an industry, however, which is intensely capital intensive. We need money all the time to produce books. It is an industry in which conglomerate takeovers and mergers have also increased rapidly over the years, and the statistics in this testimony I think will point to that fact. We are chronically short of adequate working capital. We are chronically under the gun to be either taken over or go out of business. The small publishers in

terms of numbers represent the great constituency within the AAP in terms of numbers, although not in terms of books published.

My own experience I think is similar and probably bears some explanation. We began in 1969. I had very little capital. It all came from my personal trust fund. When I went to the bank to explain what I was trying to do, they, of course, understood nothing about book publishing and were only willing to grant me a loan under a personal signature, and then two points over full prime. So the loan was fully guaranteed and I was paying two points above prime for it.

We were not profitable for 5 years, which I don't think is unusual among publishers, maybe among small entrepreneurs in general. When we finally became profitable, we switched banks and we are not getting loans at a point under prime, the small business prime, which is legal in Massachusetts. I still have to guarantee those loans personally. We have been profitable for 4 years now.

Two-thirds of our publishers go out of business within the life of the company. We have no capital available to us other than what we can generate ourselves through our business, other than what becomes available because we are taken over, which I fear, and also what is available to us through the banks. The banks, in my experience, are not interested in providing capital for expansion or for working capital. They're interested in short-term loans for short-term needs.

I want to read this letter which came from a fellow member of the AAP on page 4, because this was my experience exactly.

When we decided to start our company early in 1972, we needed to raise most of the capital from outside investors. We had been urged by some to retain control by not selling more than half the stock. Good advice it was, too, but it turned out not to be possible. We did not have enough capital, though we could have kept effective control with an SBA-guaranteed loan.

But it took a visit to the SBA office in San Francisco to get the shocking news that publishers were specifically excluded from such loans. When I made the appointment, I was greeted warmly enough—which was precisely my experience in Boston, I might add—and felt, especially with my previous experience and excellent references, that it would be a mere formality to arrange a loan for about \$250,000 (really a line of credit). But the answer was a categorical no. Fortunately, we were able to raise the necessary capital elsewhere, but only by giving away a controlling interest in the company we had worked so hard to launch. An SBA loan would almost certainly have made the difference, not to mention more time to concentrate on publishing instead of on money raising. If so many Government officials who claim their sympathy and support for small business people, entrepreneurs, and private enterprise were really to help all deserving applicants, I think it would be a great contribution to our country and its future.

From the standpoint of social utility, book publishing should be judged—I believe this categorically—on the basis of its performance, on the basis of its profits, and on the basis perhaps of its prospects. I think the SBA is a business organization; it is not there to judge values; it is not there to say what's good for America and what's bad for America. I think those could be applied just as easily to television stations or to cable stations or to any number of industries which are eligible for SBA loans as they could be with legitimate fears, which I understand, to book publishing.

I want to say, too, that everything has in a way turned from when I began to the situation now. I am referring specifically to the invisible subsidies that we got from the Government. When I

started publishing books, we could ship a book anywhere in America for 14 cents for the first pound and 3 cents for each additional pound. That rate now has gone up. We are no longer a preferred class of citizen. It now costs us 63 cents for the first pound and 24 cents for each additional pound up to 7 pounds. That's an enormous increase. It means that to ship a 2 pound book it has gone from roughly 17 cents to almost a dollar.

In addition to that, education and literacy are no longer, in any way that I can discern, a part of the national agenda. Moneys which were available for libraries to buy books, moneys which were available for teachers to buy books, for school systems to buy books, have evaporated under the title IV program. We no longer can count on the sale of the most legitimate books to libraries. That has evaporated as a source of income for us as publishers.

I think the stated fears of the SBA, that the Government might be embarrassed if the loan were made to an existing book publisher or someone who wishes to enter the field of book publishing, because it might appear that the SBA was infringing on the freedom of the press, is really an absurd argument. I just can't buy it. You make loans to other industries; you make loans to cable TV companies. I go to motel rooms and you know what is available through cable TV as well as I do. Is there a public outcry on that basis? Do you Congressmen get letters from your constituents saying "My God, I just was in a vibrator bed and saw a dirty movie on the TV and you loaned them the money?" I can't see that really happening.

I think, if you are really concerned with it happening, you can control it. You can contractually obligate the publisher, or the SBA, for that matter, not to interfere in editorial decisions. I think there are ways around it.

When you make a loan to a radio station, for instance—as I understand it, I guess this comes under control of the FCC, so you're pushing it off into another organization—but surely there could be a mechanism whereby if they went out of business, a legal default mechanism could be put in place which would protect the SBA from any embarrassment about the default.

I think the big difference, just to condense this—because I would rather answer your questions if you have them—is that we in the book publishing industry, and I personally, are very concerned with the remainder of the bill set forth in section 2, which states that the SBA may deny financial assistance to any small business concern described if the assistance will be: One, adverse or detrimental to a legitimate public interest, or two, used primarily to promote or criticize political or religious issues. I just have a lot of trouble with that. I don't know how you define what is the legitimate public interest, other than the classic definition, which I think applies to commerce, and that is that what the public has a need for and what there is a market for, business has an opportunity, if not a responsibility, to provide.

We keep coming up with the example of the Daily Worker. There is a good reason why the Daily Worker hasn't published for 20 years, and that is because nobody bought the newspaper. That is why the Daily Worker is defunct. So, to me, that whole issue is a red herring. If you believe in free enterprise, if you believe in oper-

ating in the marketplace, I think you have to take your chances with the marketplace. The Daily Worker took that chance. With or without an SBA loan, I think it would still be defunct today.

I would urge the chairman and the members of the committee to study this problem. It is a longstanding problem and it's a problem, at least with you people, for which there is now a glimmer of hope of solution. I trust that in the interest of continuing free and open competition in the field of book publishing that positive steps might be taken to reverse this position.

I think—and this is my addenda—that this small corner of free enterprise is terribly important. I happen to think it is more important than movies. I happen to think it's more important than newspapers. I think books are the real molders of opinion in this country. They are the disseminators, they are the software for the other industries, and that it has been a real pity that for this pettiest of bureaucratic reasons publishers have been denied—good publishers, responsible publishers, publishers who aren't publishing pornography, or politically activist tracks, but the broad general range of criticism, discussion, and dissent which comes under the category of any responsible publisher's list—any aid from the Government. Let us judge publishers as we judge all businesses, on the basis of their performance and the basis of their prospects, not on some dimly defined fear of embarrassment or of their roles as movers of society.

Thank you.

[Mr. Godine's prepared statement follows:]

PREPARED STATEMENT OF DAVID R. GODINE, PRESIDENT, DAVID R. GODINE PUBLISHER, INC.

Mr. Chairman, I am David Godine, President of David R. Godine Publisher, Inc. of Boston, Massachusetts and I appear today on behalf of the Association of American Publishers, Inc. (AAP). AAP has about 300 members, who account for over 85 percent of all books published in the United States. Our members range from very small, single-entrepreneur operations and family-owned companies to larger closed corporations, sizable publicly traded companies, and very large communication conglomerates.

Until January 1978, the Small Business Administration consistently refused financial assistance to all enterprises involved in the dissemination of "ideas and values". This was a policy adopted by the SBA without mandate from Congress in the belief that SBA would thus avoid any appearance of governmental interference with freedom of expression. On January 27, 1978, however, SBA modified its policy to include loans to the electronic media (radio and TV), but continued to exclude the print media, books, newspapers, magazines, etc., without acknowledging a basic inconsistency.

The stated SBA position is to avoid government interference, or the appearance thereof, with the constitutionally protected freedoms of speech and press. We contend that SBA regulations, as they now stand, are fraught with inconsistencies, that the different treatment accorded different categories of "opinion molders" raises precisely those constitutional questions which the SBA has been professedly trying to avoid.

The number of active book publishers serving national and international markets is now greater than ever before in our history. Good books have never been in more plentiful supply and have never reflected greater diversity of subject matter or treatment. By every significant measure, book publishing has experienced uninterrupted growth for at least 45 years. The number of publishing establishments has grown from a low point of 410 during the Depression of 1933 to 1,744 in 1982, of which 1,398 were companies with fewer than 20 employees. The number of new titles published each year rose from 15,000 in 1960 to 38,526 in 1982.

At the same time, most book publishers are small businessmen who are chronically short of adequate capital. Acquisition and merger rates in book publishing have

been historically two or three times higher than those of the industry as a whole, a condition which reflects, in part, the fact that small publishers (who comprise the great majority) have difficulty borrowing money to finance normal growth. They start on a shoestring, and when they make progress the only way to underwrite a growth in sales is to merge.

Book publishing fully meets the First Amendment intention described by Judge Learned Hand as reliance on "a multitude of tongues". On the other hand, book publishing is a financially precarious enterprise for most participants, and the SBA policy of denying loans to publishers is probably contributing to the unusually large number of mergers in this industry. A more socially positive SBA policy could strengthen the First Amendment.

About 100 book-publishing enterprises are started each year; two-thirds of them go out of business over the active life-span of the founder—meaning about 20 to 30 years. Success creates demands for more operating capital to support more and larger author's advances, larger inventories, and larger accounts receivable. Most small companies cannot by themselves raise the money needed to sustain growth, or even to assure survival in lean years. With SBA borrowing precluded, merger is the main road to carrying on the business beyond the first generation. But in many cases a loan on reasonable terms would be a better solution because it would obviate the need to dilute ownership.

Sometime ago AAP received a letter from a small publisher in California who stated:

"When we decided to start our company, early in 1972, we needed to raise most of the capital from outside investors. We had been urged some to retain control by not selling more than half the stock. Good advice it was, too, but it turned out not to be possible. We did not have enough capital, although we could have kept effective control with an SBA-guaranteed loan.

"But it took a visit to the SBA office in San Francisco to get the shocking news that publishers were specifically excluded from such loans. When I made the appointment, I was greeted warmly enough and felt, especially with my previous experience and excellent references, that it would be a mere formality to arrange a loan for about \$250,000 (really a line of credit). But the answer was a categorical no. Fortunately, we were able to raise the necessary capital elsewhere, but only by giving away a controlling interest in the company we had worked so hard to launch. An SBA loan would almost certainly have made the difference, not to mention more time to concentrate on publishing instead of on money-raising. If so many government officials who claim their sympathy and support for small business people, entrepreneurs, and private enterprise were really to help all deserving applicants, I think it would be a great contribution to our country and its future."

From the standpoint of social utility, book publishing ought to be judged by the extent to which it has enhanced the national culture, or at least the national knowledge. A basic measurement of this social contribution is the number of new titles brought out each year, and the relationship of this number to each potential reader and potential author. As previously mentioned, the number of new titles continues to rise, affording an abundance of opportunities to authors and a wide range of choice for readers.

The stated fear of SBA that the government might be embarrassed if a loan were made to an existing book publisher, or someone who wishes to enter the field of book publishing, because it would appear that the SBA was infringing on freedom of the press, is absurd. The SBA can by regulation and contractual arrangement ensure that it does not in any way influence editorial content or end up owning a publishing house. For example, SBA now makes loans to the electronic media, radio and television stations, but SBA would not qualify as a licensee to own such a station in the event of a foreclosure or default under the loan. There is no obstacle to devising arrangements for comparable safeguards in the case of a defaulted loan to a small book publisher. For example, the business could be sold at public auction.

AAP is also aware of H.R. 1157, introduced in the 98th Congress by Congressman Addabbo, which would restrict the authority of the SBA to deny financial assistance to any small business concern solely because the primary business of such concern is book, newspaper, magazine, greeting card, or history calendar publication or distribution; radio or television broadcasting; film, record, or videotape production or distribution; instruction or tutoring academic subjects; or any similar operation.

AAP endorses this concept but is concerned with the remainder of this bill as set forth in Section (2), which states that SBA may deny financial assistance to any small business concern described if the assistance will be "(A) adverse or detrimental to a legitimate public interest, or (B) used primarily to promote or criticize political or religious ideas."

We submit that there is no definition of a "legitimate public interest" and it would be all too easy for anyone to determine for some vague reason that assistance would be "adverse or detrimental" to this undefined public interest.

While we appreciate the fact that the language proposed in H.R. 1157 states that the funds can be denied if they are to be used, "primarily" is included as a safeguard, we nevertheless are concerned that many publications may directly or indirectly promote or criticize political or religious ideas. Any publisher who publishes a wide variety of books will include in its publishing list books covering political or religious ideas. Can the SBA then say that this is to be prohibited and disqualify that publisher from obtaining a loan?

Mr. Chairman and Members of the Committee, we commend you for your interest in this problem, and we hope that in the interest of continuing free and open competition in the field of publishing that positive steps can be taken to reverse the SBA's position concerning "opinion molders".

Mr. IRELAND. Thank you very much.

Let me make a statement to you based on some of the discussion of your personal experience with banks and the SBA and ask you if you agree to it.

First, an opinion. In my opinion, a great part of our problem is not only this but in all of small business activity relating to the SBA. What I would like you to reflect on and react to, and you may agree or disagree, is what I consider one of our great problems. It seems to me it is not the majority of our elected officials, my colleagues, other people in Government, the executive branch, or the public, but its both those in and out of business that have a difficult time with the concept of capital. By that I mean capital is ownership and capital is not a loan.

In my view, this leads to a real problem. In the early 1930's we realized there was a substantial difference in what we thought was getting us into trouble and we separated our commercial banks, that is, the lending aspects of them, away from the underwriting and investment in capital part. We categorically made it illegal for a commercial bank in this Nation to be in the business of investing in ownership. So, too, would I tell you that there is nothing in the SBA law that will permit it to own anything. It cannot invest, and therefore, it is not in the business of putting up capital. It's in the business of making loans. So, too, are our banks; I used to be a banker.

Incredibly, our mindset in this country is that banks continue to be the source of capital. They're not a source of capital. They're a source of loans. Every young loan officer coming up in the bank is taught, "don't make a 'capital' loan; you're not investing in the business; you're making a loan to the business." Yet we have all the private sector, all the SBA, everybody going to the SBA saying, "We're looking for capital."

Then we get people like yourself in there saying, "You know, I want to go out and get capital. What I want is capital from a bank so I don't have to give up ownership." But capital and ownership are one and the same thing. So what you wanted from that bank, or from the SBA, was a loan, not an investment, not capital, so that you could retain the ownership. A wonderful idea. I'm all for it.

It seems to me our problem is that in the guts of dealing with the SBA and lending we have a misconception of what we're talking about. Because if we were to address it, that the SBA, in making its loan or in anything that it does, it cannot in any way

have any ownership. It is not there for ownership any more than our banking industry is allowed to have ownership in America. Therefore, what difference does it make as long as they make their loan to someone in theory that can pay it back based on a judgment of the circumstance. What on earth does it have to do with whether they are endorsing it, being the Daily Worker or a pornographic movie house or a motel or a publishing company that puts out a dirty book?

So it would seem to me that if we had a true concept of what capital and ownership is, versus what a loan is, it would mean that in truth this legislation would be correct. This would mean that the SBA has no business having an opinion molder rule at all.

How would you reflect on that, having had the experience that you have?

Mr. GODINE. I accept the distinction between capital and loan, from bitter experience at the bank—and believe me, having had it explained to me many times. I also think that having heard your questions I understand much more your predicament, and I see that it is not a clear-cut case. We have a responsibility I think to the first amendment to protect freedom of expression and freedom of speech, which the AAP stands for and which I believe in. I think you also have a responsibility to your constituencies not to do something which is offensive, with what is I think their money. I construe that from your comments, that you're loaning public money, or you're guaranteeing it.

Mr. IRELAND. But in a sense, as a loan, you don't have any control and you don't have any ownership. Therefore, why wouldn't you be absolved from the unsavory activity of that company as long as it pays that loan back?

Mr. GODINE. You are. I don't understand the question.

Mr. IRELAND. Well, I'm saying that would totally support doing away with this rule by the SBA.

Mr. GODINE. I don't see the point of the rule, because I believe enough in the free marketplace to believe that sooner or later—I have seen it happen in my own community, I have seen it happen in Boston—these companies which you people would probably consider socially unsavory, but politically would have to admit their right to exist, have been hoisted by their own petard. I mean, they have failed and have failed consistently again and again. Any bank officer looking at those companies would probably come to the same conclusion, and any SBA loan officer would come to the same conclusion.

Just as I think in the early days, if we had gone for an SBA guaranteed loan, we wouldn't have gotten it, and deservedly so. But right now there would be a big difference to me, paying prime or a point over prime, and looking for, let's say, \$100,000 in short-term money, going to my bank, which God knows is very sympathetic, and going to the SBA.

I don't even know your policies, but I can't believe that it would not be advantageous for me to have that loan guaranteed by the SBA, even assuming I were willing to guarantee the whole loan with my personal assets, which is what I'm forced to do at the bank anyway. Am I wrong?

Mr. IRELAND. I think you state the facts correctly, and I appreciate that. I think that gets to the heart of some of what we're doing here.

Mr. Bilirakis.

Mr. BILIRAKIS. Mr. Chairman, I, like you, am a free enterpriser. I suppose that might somewhat belie some of the comments we made up here. But I also accept Mr. Godine's explanation that he understands the predicament that we have, that we represent constituents and it is their dollars that are being loaned and are being used for some of these purposes. So we have got to be certainly cognizant of that, too. SBA is not a business. It is a lending agency, circulating, if you will, taxpayers' dollars. We have got to be concerned about things that probably a bank or a private lender would not be as concerned with.

Thank you, sir.

Mr. IRELAND. Thank you.

Mr. SCHMIDT. Mr. Chairman, we would ask that Mr. Godine's full statement be included in the record.

Mr. IRELAND. Yes, indeed. We will do that, without objection. Thank you for being with us.

Mr. Riekes, could I ask you one additional question, something we didn't get before?

Mr. BILIRAKIS. Excuse me, Mr. Chairman. I don't believe that Mr. Riekes asked that his full statement be placed in the record, and I think he probably intended it to be. He sort of paraphrased it and intended that to be a part of the record.

Mr. RIEKES. Yes, sir, I would.

Mr. IRELAND. We will, indeed, do that. Without objection, we will have everyone's statement in that fashion.

Let me delay you for one moment and ask you one more question. We haven't touched on what I guess you would call the religious area of this. This would definitely have an impact on greeting cards. If the Federal Government, according to the Constitution cannot set up a church or support churches, can they, through the SBA, be in the business of publishing Bibles and printing Christmas cards or anything of that kind? How do you deal with that kind of problem?

Mr. RIEKES. I think the language of Mr. Addabbo's bill was not too clear on that, so in our suggested amendments, which is being used by the Senate, we use a phrase that the courts have used frequently, that is that an applicant could not get a loan if it will primarily be used "to advance or inhibit religion." That would be an excluded category. That doesn't mean it's an unlawful business; it means only that because of the nature of our Constitution we just could not get involved in that area.

Mr. IRELAND. That would touch on Easter cards, Christmas cards, et cetera?

Mr. RIEKES. I mean, if the business was primarily engaged, let's say, in selling religious artifacts of some kind, that would not be a qualified applicant in my opinion. If somebody produced greeting cards and among the greeting cards they produced things that mentioned merry Christmas, then it wouldn't be primarily engaged in a religious thing. It would just be along there with the happy anniversary and happy birthday.

Mr. IRELAND. That's good. I think that was important for our hearing record.

Mr. Bilirakis, do you have anything else?

Mr. BILIRAKIS. No. I suppose we're saying, then—and maybe rightly so, I don't know—that a religious bookstore which deals strictly in religious materials would not be eligible.

Mr. RIEKES. Yes. That is because of the way our Constitution is structured. We just have to accept that. It is no criticism of those stores, but we just have to deal with that issue.

Mr. IRELAND. That's good.

Mr. BILIRAKIS. Thank you.

Mr. IRELAND. Thank you very much.

We're adjourned.

[Whereupon, at 11:30 a.m., the subcommittee adjourned, to reconvene subject to call of the Chair.]

SBA'S OPINION MOLDER POLICY, AND H.R. 1157

WEDNESDAY, MARCH 7, 1984

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON EXPORT OPPORTUNITIES AND
SPECIAL SMALL BUSINESS PROBLEMS,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:30 a.m., in room 2359-A, Rayburn House Office Building, Hon. Andy Ireland (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN IRELAND

Mr. IRELAND. Good morning everybody. We are here today for our second hearing on the subject of Small Business Administration's opinion molder policy.

The first hearing on the subject was held last November 15. The opinion molder policy was established by the SBA's own policy board at the inception of the agency, continuing the same policy established by its predecessor the Reconstruction Planning Corporation.

This rule prohibits help for a business engaged in the creating, organization, expression, dissemination, promulgating, or distribution of ideas, values, thoughts, opinions, or similar intellectual property, regardless of medium, form, or content.

The bill introduced by our colleague, Representative Joseph Adabbo, H.R. 1157, is currently pending before the subcommittee.

This bill would restrict the authority of the SBA to deny financial assistance to small business concerns solely because the primary business operations of such concern relate to the communication of ideas.

At the last hearing the subcommittee heard the witnesses who opposed the SBA policy. The witness list included representatives from the National Association of Theater Owners, the National Association of Concessionaires, the Theater Equipment Association, the Greeting Card Association, and the Association of American Publishers.

Today we will hear from the SBA and parties who support these opinion molder policies. After we have heard testimony from both sides of the issue the subcommittee will meet to decide whether these changes in the rule are necessary.

I would be delighted to hear from you, Mr. Vandergriff.

**OPENING STATEMENT OF HON. TOM J. VANDERGRIFF, A
REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS**

Mr. VANDERGRIFF. Thank you, Mr. Chairman. I want to commend you relative to providing us with this opportunity to discuss the opinion molder policy. I am very interested and concerned about this matter, and when the SBA testifies today I will outline certain problems I have with this policy. When it was first brought to my attention, I communicated to the SBA that the proposed business—a motion picture theater in the small community of Sulphur Springs, TX, where none currently exists—was an enterprise supported by the chamber of commerce, the community, and by various local business interests. As I understand it, at least, the regional office of SBA was optimistic about the support and tentatively granted approval of the project. Then, it was overruled by the Washington office because of the very policy we are discussing today, so I have my own problems with the policy.

I'm interested in exploring modifications of the opinion molder policy that might be possible, reasonable. Therefore, I am looking forward to the testimony of our witnesses today, and thank you for holding the hearing.

Mr. IRELAND. Mr. Torres, have you any comments?

Mr. TORRES. Thank you, Mr. Chairman. No comments this morning. Just move along and let you open up the hearing. Thank you.

Mr. IRELAND. Our first witness is the Administrator of the Small Business Administration, Mr. Sanders. Please join us. We're delighted to have you before us again.

**TESTIMONY OF JAMES C. SANDERS, ADMINISTRATOR, SMALL
BUSINESS ADMINISTRATION, ACCOMPANIED BY CHARLES
HERTZBERG, DEPUTY ASSOCIATE ADMINISTRATOR OF FI-
NANCE AND INVESTIGATION, AND MARTIN D. TECKLER, AS-
SISTANT GENERAL COUNSEL, OFFICE OF LEGISLATION, SBA**

Mr. SANDERS. Thank you, Mr. Chairman. It is a pleasure to be here.

If I may, Mr. Chairman, I would like to read my written statement.

Mr. IRELAND. Yes, sir.

Mr. SANDERS. It is a pleasure to be here today to present the Small Business Administration's position on H.R. 1157, a bill to restrict the application of our so-called opinion molder policy.

The opinion molder policy, codified in paragraph 120.2(d)(4) of our regulations precludes SBA from granting financial assistance to any opinion molder, defined as a concern which is engaged in the creation, origination, expression, dissemination, propagation or distribution of ideas, values, thoughts, opinions, or similar intellectual material, regardless of medium, form, or content.

H.R. 1157 would amend the Small Business Act to prohibit SBA from denying financial assistance to any small business solely because its primary business operations relate to the communication of ideas. Specifically under H.R. 1157, SBA could not rely on the opinion molder policy to deny an application for a loan or a loan guarantee to a small concern whose primary business operation is book, newspaper, magazine, greeting card, or history calendar pub-

lication or distribution, radio or television broadcasting, film, record, or video tape production or distribution, theater or motion picture entertainment, or instruction, or tutoring, or academic subjects.

The bill would, however, retain the opinion molder policy in two types of cases: First, where the financial assistance would be adverse or detrimental to a legitimate public interest; second, where the loan proceeds would be used primarily to promote or criticize political or religious ideas.

Before I discuss the purposes and background of this longstanding policy, let me say that we welcome the congressional guidance in reconciling the agency's statutory purpose of fostering the growth and participation of small business in the market with possible unconstitutional interference with the freedom of expression.

There are three basic reasons why the agency has maintained the policy: First, to avoid Government interference or the appearance of such interference with the constitutionally protected freedoms of speech or press by subsidizing the publication of ideas which promote particular political views or propaganda or advocate certain religious tenets.

Second, to avoid the possibility of creating an unconstitutional prior restraint on the expression of ideas by our applicants. This could come about, for example, if a media applicant altered the content of its publication in the belief that it would enhance its chances of obtaining financial assistance. Conversely, once a media small business obtained SBA financial assistance, fear of Government reprisal might cause it to alter the content of its publication. Both could be construed as examples of unconstitutional prior restraints.

Finally, as a matter of providing for the most beneficial utilization of available budget authority, SBA wishes to avoid lending to concerns which publish or produce or sell materials of a highly controversial nature, which, while not illegal, may not be in the public's interest to promote. Were the agency to attempt to make individual decisions on what is and what is not in the public interest based on the content of the communication, it may be viewed as placing itself in a censorship role.

If so viewed by a court, such a role by a Government agency would not only be unconstitutional, but in itself would not be in the public interest.

The opinion molder rule is not a new policy. It has been part of the agency policy since its inception in 1953, having been adopted by SBA's predecessor, the Reconstruction Finance Corporation.

The dilemma posed by attempting to reconcile SBA's statutory purposes with the opinion molder policy is also longstanding. Over the years, SBA has promulgated seven regulatory exceptions in an attempt to resolve the dilemma.

These include commercial or job printing firms; publishers of shoppers' newspapers or circulars composed completely of advertising material; firms producing advertisements and technical materials; firms solely involved with the reproduction of other materials; broadcasting and cable television operators; vocational, technical and other nonacademic schools, and general book or music—

record—stores and general merchandise stores which may sell books, newspapers, magazines, records, et cetera.

Now the first four of these exceptions and the exception for vocational and nonacademic schools were believed to be justified because they relate to firms which do not attempt to advocate any particular viewpoint or idea and, as such, are not in the position of molding opinions.

Since the strict regulation of broadcasting and cable television firms by the Federal Communications Commission has already been upheld by the Supreme Court, SBA excepted them from the opinion molder rule. As an additional precaution, the regulatory exception specifies that the content of their programs is not to be considered in granting them financial assistance.

Finally, general merchandise stores and general bookstores have been excluded from the opinion molder rule because at any given time, they present a wide range of topics and titles and do not advocate any particular opinion.

In recent years, there have been a large number of mergers and acquisitions in the media-related industries which have tended to eliminate many media-oriented small businesses and to promote a concentration of ownership.

SBA has been concerned with the effects of this trend. Thus, in 1980, SBA published an advance notice of proposed rulemaking in order to develop an approach to altering the opinion molder policy and to increase SBA's ability to assist small media concerns. SBA proposed seven regulatory changes in the opinion molder policy which we believed could be taken individually or in any number of combinations without fear of successful legal attack.

One, retain the present rule, but provide a waiver procedure by which media concerns which have been denied assistance could demonstrate that the purpose of the rule is not served by their denial.

Two, expand the current exceptions to the rule to allow SBA to assist those types of businesses which meet the present broad definition of an opinion molder, but which do not primarily mold opinions, and whose funding would not be likely to promote governmental interference with the freedoms of speech and press.

Three, replace the present broad proscription against assisting opinion molders with specific prohibitions against certain types of assistance to certain types of enterprises.

Four, prohibit SBA assistance to certain forms of media enterprises which advocate a particular religious, political, social or economic point of view.

Five, prohibit SBA assistance to an applicant if more than 30 percent of the applicant's gross income is derived from the sale, rental or lease of religious products, materials or services.

Six, prohibit SBA assistance to an applicant if more than 30 percent of the applicant's annual gross income is derived from the sale, rental, or lease of sexually explicit products, materials or services.

Seven, prohibit direct SBA loans to opinion molders, but allow SBA guarantee assistance to such concerns.

SBA received a plethora of comments on the proposed changes, however, and none of the proposed changes were made final. In

February 1981, SBA published a proposed rule which made general audience motion picture theaters eligible for SBA loan assistance, but which retained the opinion molder rule for purposes of specialty theaters.

Specialty theaters were defined as those which cater to limited audiences such as those showing primarily sexually oriented films or that promote or advocate ideological, political, or philosophical viewpoints.

During the comment period on this proposed rule change, a public interest organization objected to the change on the basis that any rule that discriminated against specialty type theaters based on the content of the material, for example, pornographic, political, and religious, would not be constitutional. After careful examination of the question SBA's Office of General Counsel agreed with this position.

So SBA retained its previous rule that all theaters were ineligible for assistance.

The opinion molder policy has not been changed by regulatory action in some time. As you can see, Mr. Chairman, it is not an easy issue to resolve and we welcome this subcommittee's guidance on the most appropriate way to change the current rule, if you believe that change is advisable.

H.R. 1157 would abolish the opinion molder policy exception cases where the financial assistance would be adverse or detrimental to a legitimate public interest, or used primarily to promote or criticize political or religious ideas. In analyzing whether the opinion molder policy should be abolished we must seek to obtain the most appropriate means of reconciling SBA statutory mandate with constitutional guarantees.

Any determination by Congress with respect to alternatives must include in the legislation or accompany legislative history language which further identifies the nature of the prescribed matter. A clear congressional finding as to the types of businesses which would be ineligible for our assistance would be welcome, and would greatly assist us in promulgating implementing regulations.

We must also note our concern with respect to the exception in H.R. 1157 which would establish a standard of adverse or detrimental to a legitimate public interest for SBA to evaluate financial assistance applications.

We believe that the proposed standard could be construed as unconstitutionally vague. In its place should be language which clearly defines those businesses which are adverse or detrimental to the public interest and a proscription against assistance to them.

However, any such language must balance SBA's need to make loans to only legitimate businesses with protected constitutional rights.

Finally, we object to the requirement contained in H.R. 1157 for a hearing on the record with respect to determinations by SBA of proscribed activities. Such a requirement would lead to lengthy hearings on applications for assistance each time the Agency interpreted the law adversely to an applicant. Instead we favor, as indicated above, further clarification of the proposed exceptions which would permit easier administration by our financial assistance personnel and obviate the need for hearings on the record. We look

forward to cooperating with you in order to accomplish any changes in the opinion molder which Congress sees fit to mandate.

Mr. Chairman, this concludes my prepared statement, and I'll be happy to answer any questions you may have.

Mr. IRELAND. Thank you, Mr. Sanders. There's some testimony before the Senate subcommittee in 1980, Mr. Theiste—

Mr. SANDERS. Theiste?

Mr. IRELAND. Theiste. In a discussion concerning the elimination of small businesses in the media area through merger. He indicated that the SBA was about to come out with some regulatory changes that would cover the problems of the opinion molder operation, and I wonder in this specific instance where he was talking about mergers of small media-oriented business, whether anything became of that.

Mr. SANDERS. Well, Mr. Chairman, those are the ones that I read here that we published in 1980 for advance notice proposed rule-making, and we received such an avalanche of comments that we buried it.

Mr. IRELAND. Adverse comments?

Mr. SANDERS. Yes.

Mr. IRELAND. The plethora that you had—

Mr. SANDERS. Right.

Mr. IRELAND. Before I turn it over to my colleagues here, let me ask you one further question. On page 4 you told why general merchandise stores and general book stores have been excluded from the opinion molder rule because at any given time they present a wide range of topics and titles, and do not advocate any particular opinion. In our previous hearing we heard from the greeting card people. They're quite concerned selling greeting cards that promote one thing, but unless I am going to the wrong retail greeting card places, they certainly have a large range of topics and titles involved. Why wouldn't they, for instance, fall under that same—

Mr. SANDERS. Well, that is what troubles me, too, Mr. Chairman, and since that is a very difficult question I am going to ask Mr. Hertzberg who is with the financial assistance office to answer. He is in day-to-day contact and has probably some background in denying those—

Mr. HERTZBERG. Thank you. Mr. Chairman, actually in the prescriptions on the opinion molder rule, it's greeting card manufacturers that are included. That is a publication kind of activity.

I would say that greeting card stores, unless they do specialize in a certain type of greeting card would fall under the general merchandise exception to the rule.

Mr. IRELAND. The manufacturer doesn't sell directly to the public. What he manufactures has got to go through that retail outlet, correct?

Mr. HERTZBERG. That's correct.

Mr. IRELAND. All right. Therefore, it would be widely spread unless it was covered by a single unit source, so why would they have a problem?

Mr. HERTZBERG. We don't have a problem with the retailer.

Mr. IRELAND. I understand. Why would you have a problem with the manufacturer? His product either goes widespread to the retail stores, and therefore, you have got no problems. Or it goes to a

single retail outlet that puts out nothing but that manufacturer's products and you've already said he doesn't do that.

Mr. SANDERS. Are you speaking of denying an application to a printer of cards rather than a card shop?

Mr. IRELAND. Well, the gentleman said that the card shop would be, like your testimony says, a wide range of topics in say 100 different costs. He also said that the manufacturer is governed by your opinion molder rule because he might put out perhaps one thing advocating one religious topic or one political topic or something similar. Now my question to him is having put that out as a manufacturer, he has two ways to go. He can sell that through the retail outlet in which the public is not harmed in any way because there are 99 other things besides that manufacturer's card there. Based on that logic, he shouldn't be covered by your opinion molder rule if he sells it to a store that sells 100 percent of only his political or religious thing. It is covered by the opinion maker rule from exactly what the gentleman said.

Mr. SANDERS. I don't know if we ever had an application from a manufacturer of cards.

Mr. IRELAND. Well, we apparently have because they were in here the last time screaming about it.

Mr. SANDERS. Well, you can understand that if one of them were to consistently print, say Nazi party literature, or Communist party literature, or if they advocated one philosophy or religion singularly, all the time—then assisting that would be to promulgate one religious or political point of view.

Mr. IRELAND. The point that I am trying to elicit from the gentleman is that if in doing that they have their own distribution system and are selling through a card shop and these were not advertising one single philosophy, such as people doing greeting cards for religious holidays, why should they be prohibited from manufacturing this particular item that goes through all these card shops?

Mr. SANDERS. Well, I think that would be excluded by your proposed legislation because, in my example, he is advocating one religious and political point of view. A concern which is putting out one political or religious point of view would be excluded by this proposed legislation.

Mr. IRELAND. Go ahead.

Mr. HERTZBERG. Once again there's also a difference between the publisher, himself and the retailer that is handling this wide variety. The publisher has total freedom to choose what kind of cards he wants to print, what kind of messages he wants to get across. We don't want to interfere with that right, but just as we do not aid publishers of books, although we do aid general book stores, we would not aid the publisher of cards while we would aid the retailer that would sell a wide variety of cards.

Mr. IRELAND. Mr. Vandergriff.

Mr. VANDERGRIF. Mr. Sanders, if you recall my original comments in which I made reference to the theater in Texas, you will understand why I am going to dwell on this situation some more. This town was denied a theater, and it is a long way between towns in certain sections of Texas. It is unfortunate that the local SBA officials indicated original support, but this was ultimately denied.

The community was really interested in the construction of the facility. I take it that motion picture theaters have particularly troubled SBA through the years, judging from your testimony. At one point in time you spoke in terms of support for certain types of theaters, provided you could exclude aid to other types of theaters, and that finally, the general counsel made a judgment that you should just walk away from it and continue to prohibit support to any and all theaters. You don't expand upon that to any great degree, and I wonder if you could enlarge upon the reasoning. It seems to me that what was said was that there are theaters and certainly motion pictures that would opt to take on the liberties, and yet if someone objected at all, it would be ruled off limits.

Mr. SANDERS. Well, that's true, Congressman. As you know we didn't have that proposed regulation changed. We received a strong reaction from one of the public interests, legislative group or legislative lobbyist groups, and our general counsel looked at their brief and agreed with them. Perhaps Mr. Teckler who is assisting me today as my constitutional lawyer would care to comment on that. He has some background in the history of that.

Mr. VANDERGRIFF. I'd appreciate it.

Mr. TECKLER. Yes, sir, Mr. Vandergriff; the problem there is making a determination between what would be and would not be the type of theater which we would want to benefit. Certainly under a blank rule we would want to benefit a general audience theater if we had the opportunity. We would want to avoid benefiting a theater which was involved in showing pornographic or obscene materials, for example. When we try to make that—if we were to try to make that determination—we would be putting ourselves in a position to make a determination as to the content of the films that were to be shown at a given theater, and the argument there is that we would be infringing on the constitutional first amendment rights. If we were to make a determination that while a particular theater was not showing a film which was illegal, or found to be illegal because it was obscene but was pornographic, and, therefore, possibly objectionable to the community standards and certainly to our standards, we would be imposing ourselves in the position of a court making a judgment that this is an objectionable type of film this theater seeks to show, and, therefore, we will not grant them assistance.

On the other hand, this is not an objectionable type of film that this particular theater wants to show, and, therefore, we will grant them assistance. We're trying to avoid putting ourselves in that type of position, and that was the type of argument which was sent to us when we first proposed the rule to make loans available to general purpose theaters which our general counsel's office found persuasive and which caused us to retract our proposed rule at that time.

Mr. VANDERGRIFF. I suppose I am having some difficulty with the fact that you found grounds to permit support for general book stores and record stores and radio and television stations, and yet I think we all have to say that there are, in such instances, material that is often objectionable to at least some of us. Yet you have been able to be comfortable with a general classification in those cases. Surely in motion picture theaters, even though there might occa-

sionally be a film or two that we wouldn't like for our children to see, there are others that we would see. I am having trouble in seeing a differential between those various categories.

Mr. TECKLER. Well, sir, it is a very difficult area, and the practical response to that situation is, and I don't know whether you'll find it persuasive or not, but in a given general book store, for example, there is a wide variety of merchandise on the shelves, and the customer comes in and takes what he or she desires to purchase. In the movie theater you have a situation where there's only one movie on the screen, and it may be a movie which is "R" or "X" rated but which is not illegal, is not obscene under present constitutional standards, and, is, therefore, not illegal, and is, therefore, available to the community in a given situation to view. Nonetheless we would find that type of a movie one which we would not seek to promote by advancing assistance to the theater which was showing it, and then in most instances throughout the country there are particular theaters and particular communities that show that type of film on a day-to-day basis continuously.

It is not illegal. We have it here in Washington, and we have it all over the country. It has not been found to be obscene, but it is objectionable from our standpoint, and I think from probably the standpoint of most of the members of the committee, for the Government to be assisting such a type of theater. We want to avoid that, and that is the way the opinion molder rule has been applied, and aside from the constitutional arguments which would force us into a judgment on the content of a particular theater's showings, denying assistance generally to all theaters allows us to avoid entering into both the constitutional question and the sticky question of making a determination of what is objectionable in a given community even though it may not be per se illegal. That is basically the rationale for retaining the opinion molder rule, with respect to all theaters as it exists now.

Mr. VANDERGRIFT. What is your reaction to the fact that the trend in the motion picture theater houses today seems to offer several films available by purchasing only one ticket. In other words you can gain access to a theater that might be offering, if I can remember in one case, eight films. You buy one ticket and you can take your choice of eight different films. That seems to me to be a shelf filled as would be the case in a record store, or some other type of book store.

Mr. HERTZBERG. From a policy standpoint I think that if that was enough to cause us to reexamine or get us to reexamine the general book store rule, and see if that would overcome the objection, as Mr. Sanders indicated, we had sought a way to make general audience theaters eligible under the opinion molder rule. It was the argument that we would be exercising a censorship role to exclude them, the specialty type of theaters that caused us to withdraw the rules change.

If we could reexamine that I think we would be able at least to make another attempt to change the rule.

Mr. TECKLER. Yes; from a legal standpoint again we had come forward with the proposed amendment, and it was this argument that we would be examining the content that caused us to withdraw. If we can avoid that constitutional argument and also avoid

involving ourselves in circumstances which are blatantly objectionable where the Government shouldn't be involved, that is something which we'll have to wrestle with in terms of developing a standard.

We wanted to make the change, but the constitutional argument is persuasive when you talk in terms of involving an agency of the Government in examining the content of a given film. The courts can't agree on what is or isn't obscene, and were we to try to make those judgments for the courts, we think we would be clearly exceeding our limitations as an administrative agency, and then, again if we make a determination that something which has not been found to be illegal in a given community is nonetheless still not eligible for our assistance, we again would be probably exceeding our legal limitations in terms of the Constitution.

Mr. VANDERGRIF. I've taken more of my share of time, and I would continue, but I submit again respectfully the idea that with one ticket you have access to several films, and I submit that this might be worthy of your consideration. Mr. Chairman, thank you.

Mr. IRELAND. Yes, indeed. Mr. Torres.

Mr. TORRES. Mr. Chairman, I don't have any questions at this time.

Mr. IRELAND. Mr. Stenholm.

Mr. STENHOLM. No questions.

Mr. IRELAND. Mr. Roth, we're glad you are with us.

Mr. ROTH. Thank you very much, Mr. Chairman. I don't have any questions, but I'll take a look at the testimony here as we go along, and maybe I will have some questions after a while.

Mr. IRELAND. I have one last question, Mr. Sanders, if you will. It's been very clear that not only in your testimony but in what we've heard before that under the opinion molder rule there is an exception for commercial broadcasting, radio and television, and cable vision—an exception because they're under the regulatory jurisdiction of the FCC. Now how about the rationale of why that is so—is it just simply because that it takes the onus off the SBA? Certainly all these things that you weigh so heavily from a constitutional point of view are still prevalent whether the FCC is regulating them or not. Perhaps a further explanation is necessary.

Mr. SANDERS. Well, you know, I think the FCC has to be concerned with the breaches of constitutional rights and the regulation of those outlets, so we don't have to be involved. The others, there are no regulatory agencies over them.

Mr. HERTZBERG. Yes, sir, Mr. Chairman, along those lines the Federal Communications Commission must make a finding that those types of business desire is consistent with the public convenience and necessity before they're granted a license, I believe and must continue to be so while they are operating. They're subject to the scrutiny and the oversight of the Federal Communications Commission.

Mr. IRELAND. My question is when ABC television is obviously a molder of public opinion, and quite within the jurisdiction of the FCC, the FCC is not doing that which you have just told me. Yet the opinion molder rule that you have is based on the very foundation of whether somebody is molding opinions or not. It looks to me like this is kind of a cop-out operation. But I think the people that

are making that point will see—unless you have got something in your bag of tricks—that you have got a good point. The FCC does not claim that it is in charge of whether a radio station is molding opinion or not.

Mr. SANDERS. They do have to be concerned about the constitutional issues of the freedom of speech and infringement.

Mr. IRELAND. Yes; but that isn't the whole thing. You're talking in your opinion molder rule about whether you're molding opinions, and that is the foundation on which your rule was based.

Mr. SANDERS. Well, I think most of these objections that we ran into in these proposed changes that we abandoned were based on constitutional reasons. I mean they were all to do with opinion molding, certainly, but what we keep running into is this constitutional question. I urge each of you to reconsider.

Mr. IRELAND. I am saying that the FCC is not the great umbrella that perhaps you think it is.

Mr. HERTZBERG. It is a difficult area. When this policy was changed, I believe it was in 1977, there was not complete agreement on whether or not this was an appropriate change to make. I really can't say too much as to the full rationale at the time. I would tend honestly to agree that it does raise some questions. I think that there has been very little significant impact by the opening of our financial assistance programs to radio and television stations, basically because of the cost of establishing radio and television stations, and the dollar limitations of SBA loans. We have actually provided assistance—but as far as opinion molding is concerned we exercise no control over the opinion molding activities of radio stations. We can look at the FCC to control those elements of their activity that may not be in the public interest, the standards of decency and this sort of thing. It's really a very difficult situation to be in as far as we're concerned.

Mr. IRELAND. Gentlemen, any other comments or questions?

Mr. ROTH. Mr. Chairman, we had a hearing, a very interesting hearing on November 15 on this issue. And does, on—the small business—the SBA make loans or help people with theaters in our local communities now?

Mr. SANDERS. With what?

Mr. ROTH. Theaters, the building, theaters in local communities?

Mr. SANDERS. No; we're proscribed—that was what we were discussing, the difficulty of dealing with the general audience theater as distinguished from the specialty theater that may have sexually oriented or politically oriented productions.

Mr. ROTH. Your view is and your opinion is that you're not interested in making all those theaters?

Mr. SANDERS. Well, we'd like to, but we don't seem to be able to get around our constitutional problems. When we decided to just proscribe against the specialty theaters, and allow the general audience theaters to be financed, we received from a public interest group a brief on why it was unconstitutional to do this. It put us in the censorship business, and after reviewing it we agreed that legally they were on firm ground and we weren't. It doesn't do us any good to adventure out there and then get it all clobbered later on a constitutional basis. There's another attendant problem, and we don't have any solution to that. We can finance a card shop or

something like that or a book shop on the basis of their general operation, and after they have a loan they can turn into a specialty operation, and there isn't a lot we can do about it.

Mr. ROTH. Mr. Chairman, since our meeting, on hearing of the November 15, my mind's eye has been focused on this issue somewhat, and as I was going around the country, not only my home State but some of the other areas, as I drive through smaller towns I find that places of business that are closed down are usually the local theater because TV, combination of cable and the like, and I think there's also another ancillary issue that arises here, you know, most of the people asking for these types of loans especially in the area of theaters, I am sure, will become a problem—more marginal areas as far as participation as far as a local community would be concerned—wouldn't have the market, and these loans as far as the theaters, may not be the best when it comes to taking a look at some of the default.

Mr. SANDERS. Well, yes, that is another consideration you have to make, whether it is financially sound or not. I am in sympathy with the need to help these kinds of theaters, general purpose theaters, in these small towns around the country, but probably of the size that the Small Business Administration should be concerned with. Maybe you can give us some help in drafting this legislation, write it constitutionally so it would not be subject to overturn.

Mr. ROTH. Well, if there is anyone that can write that legislation or help you with it is our chairman of this subcommittee, because I've talked to him about some of these issues, and I think he's probably the most knowledgeable person I've talked to in this area of opinion molder and the like, so I think that you will be in good hands by listening to our chairman of this subcommittee.

Thank you.

Mr. SANDERS. I am pleased to hear that.

Mr. IRELAND. I note the distinct presence of some side work delegation around here, not only up here but down there.

Mr. VANDERGRIF. Mr. Chairman, could we ask if they have an opinion of S. 2084. It also speaks to restricting the policy, are there any reactions you want to give us to that legislation?

Mr. SANDERS. I'm going to let Mr. Teckler speak to that, Congressman. I'll be briefed on that Friday.

Mr. VANDERGRIF. I see. Does that mean you'll be in a hearing before then on Friday?

Mr. SANDERS. Yes.

Mr. VANDERGRIF. I see.

Mr. TECKLER. Yes. We'll be testifying Friday on that bill, and it is quite similar to this one, with a couple of small technical exceptions, and I think the testimony will be about the same, Mr. Vandergriff. If the opinion molder rule is to be changed, we would seek congressional guidance as to how it should be changed.

If there's a change to make it from an absolute exclusion of opinion molders to one which permits loans to opinion molders with exceptions for certain cases, we'd like to have those cases more clearly spelled out so that the legislation and our administration of it would not be subject to the types of constitutional attacks which we talked about this morning, and we find some faults from that standpoint with that bill which we will discuss with the Senate

committee on Friday, and seek their guidance as well and volunteer our own participation in working with both committees to try and draft, redraft a bill in a way which does not subject it to the types of constitutional attacks which we spoke of this morning, and allows us to get the assistance to the types of business which you have discussed with us this morning if that becomes permissible under a new statutory opinion mold rule.

Mr. VANDERGRIF. Thank you.

Mr. IRELAND. Thank you, Mr. Sanders. We're delighted to have you before us again. Good luck on Friday.

Mr. SANDERS. Thank you, Mr. Chairman. I'm sure we'll be in the same kind of conversation, and I'll certainly look forward to any assist that you can give us in resolving these problems. Thank you.

Mr. IRELAND. Our next witness is Davis Lee Kennedy, editor and publisher of the Gaithersburg Gazette, Gaithersburg, MD. Mr. Kennedy, we're delighted to have you here. My colleague, Mr. Barnes, has sent his regrets. He had in mind being here to give you a glowing introduction. We'll extract that from him and put it in the record.

Mr. KENNEDY. It's just before an election. He's running for re-election.

Mr. IRELAND. That's right. He's in El Salvador, I believe.

Mr. KENNEDY. Well, partly. Our newspaper does not circulate there, but we do mold opinion.

Mr. IRELAND. Yes, indeed. We're delighted to have you here. We will, without objection from my colleagues, put your statement in the record, and you can take off from there.

TESTIMONY OF DAVIS LEE KENNEDY, PUBLISHER AND EDITOR, GAITHERSBURG GAZETTE

Mr. KENNEDY. Well, first I'd like to thank you very much for inviting me, and tell you that I represent no other newspapers other than my own, and it's always an honor to testify before a committee of the House.

I am just going to go over my statement, and I'll try not to read it as your most able staffperson suggested I not, but I think there is a real problem having the U.S. taxpayer aid small newspapers in a direct form.

If you want to talk about better policing of the antitrust laws or possibly changing the antitrust laws to protect us from certain predatory practices, that we would welcome.

If you want to have a very neutral-type assistance for us through the post office, that is another type of help, but that would not, in any way, allow the Government directly to influence us.

The press in this country is a most unusual business. We're the only business that is protected by the Constitution specifically or actually by an amendment to the Constitution. An example of how unusual we are is that in the State of Maryland if I were to know that one of you gentlemen had approached one of our staff members about somebody doing something untoward, nobody could force me to reveal who had given me the facts. Now Maryland has a very strict shield law. I believe it is the strictest of just about any

State, but no other business has that kind of protection, and there is a good reason why we are treated specially.

Governments the world over, sometimes it's in a small community, and sometimes it is Uncle Sam, certainly in El Salvador, want to get across their version of the unvarnished truth. I am sure that the members of this committee have had some disagreements with some of the reporters representing some of the papers in your districts. I don't happen to know where any of you are. I know that you're from Florida somewhere, but that is it.

And I would see a problem if the members of a committee such as yours were thought of as being able to influence the Small Business Administration to not renew a loan or to grant a loan to a competitor. If you remember the pressures that the Nixon administration tried to put on the Washington Post during the Watergate coverage, they actually, as I understand it, threatened their television licenses because they didn't like the Washington Post version of the truth. Some of the rest of us often don't like it, but it is not appropriate in my opinion, for the Government to be in a position to pressure somebody in the newspaper business.

The Small Business Administration is no exception. I believe it was 2 years ago, but it might have been 3, a small weakling in this area called the Washington Business Review published a series of stories about a purported scandal in the Administration. Don't ask me any questions about the scandal, because I am not familiar with them, but according to that particular newspaper's reports, the Small Business Administration was, in my opinion, not completely forthright when it came to answering the charges.

Now how would it be if the Washington Business Review were to go right after having charged the Small Business Administration with doing something it shouldn't be doing, how would it be if they, then, went and said, could you extend my loan. There would be a feeling on the part of the Business Review, that they better be pretty careful about playing up that story. The reason is the possibility of pressure.

The Small Business Administration has the objective of aiding, counseling, and assisting the interests of the small business community, but it certainly does not have the objective of influencing the opinions of the governed about the Government. I don't think it is the position of any paid bureaucrat to do that. We have the Members of Congress and the President to try and influence us, but I don't think it is the position of those whom we, the taxpayers, pay to try and influence our opinions about legislation or about the quality of their exercising their mandate that has been given by the taxpayers' representatives.

Some newspapers that I have read are absolutely tasteless. I remember when I was in college, I don't know—I guess the guy who was in the same dorm as I was in the year before, was a real right-wing kook, but we got something called from the Mothers Mobilized for America that was just awful hate propaganda. I don't think that this type of literature ought to be banned. Back in the 1780's and 1790's the press was pretty scurrilous, and that was when they passed the first amendment but that type of publication can't—should not be banned, but it certainly should not be aided by the taxpayers. I don't think Hustler magazine should be banned,

but at the same time, I don't think that a local Hustler magazine type of approach—maybe with local beauties ought to be given Government assistance.

The press is really somewhat like the church. To maintain our independence we, in my opinion, cannot receive any direct governmental aid for a specific publication. Now if you are talking about a postal rate that is another question because that is open for all publishers including the scurrilous and the Hustler magazines and everything else. This is why the Founding Fathers so wisely protected both the press and the church from governmental harassment, thanks to the first amendment.

In the case of the Washington Business Review and the Small Business Administration, the potential of a conflict of interest is rather obvious. What, let us say, if one of your local newspapers were to accuse one of the members of this committee of doing something untoward, and this same newspaper, were the recipient of a Small Business Administration loan. It would strain my credulity to think that at least one former member of this committee in its history—I am not sure none of the current members, but some past member or maybe some future member wouldn't try to use his or her influence.

Now one of the gentlemen who testified in behalf of this legislation said, well, the Small Business Administration can't cancel a loan except for default. Well, I am in and out of my bank constantly as we buy some equipment and we pay off the loans. We're a small company. We don't have a financial vice president whose job it is to make sure we're not in default. Technically, we might well be in default of some loan if we're supposed to keep compensating balances of such-and-such an amount, and if we have to pay our printer's bill a day early, we might not have kept those compensating balances on that particular day but the next day we more than made up for it. It is easy enough to find a default if a lender wants to, particularly when you're dealing with a small company that doesn't have somebody who is spending all this time guarding against a default, is trying to sell the product or produce the product or do whatever the main purpose of the business is. There is, I think, also a fear that if, let's say we were a newspaper strongly opposed to Mr. Barnes and if it were possible for the Small Business Administration to make loans I could see where some local would-be publisher might go to Mr. Barnes and say, look, why don't you help me get a Small Business Administration loan. Mr. Barnes has excellent constituent service, so he'd certainly put all the pluses for him, and that would have some threatening influence on the current press. The fact that there would be a fear that the gentleman whom we are giving a little bit of mild hell to would be able to use Federal funds to return the favor, and I don't think that would be very healthy. Now I've summarized the main reasons why I think this legislation should be rejected. I see I've missed one of them, and this is particularly true, I guess, for the President because he probably has a little more influence on the Small Business Administration than a Member of Congress would, but now, if I might, I'd like to answer some of the points raised by the proponents of this legislation. Mr. Addabbo, I hope I am pronouncing it properly, has pointed out that the opinion molder rule

has been ignored in cases where other agencies of the Government regulate the media. I think that Mr. Ireland, you asked some very pointed questions of the gentleman from the Small Business Administration on this point, and this, in fact, presumably has allowed some financial assistance to opinion molding businesses. In my opinion, talking about opinions, the opinion molder rule should be applied to radio stations and television stations where they are broadcasting news and public events. If it is an all sports station I don't see any problem with it. If it is an all music station, all classical music or all rock or something like that, I see no problems with it. If they are broadcasting in their format news programs, I do see a problem with it.

He's also mentioned that affected small businesses engaged in the communications of the ideas, have strongly opposed the rule and criticized the administration's application of it. Might I answer the sponsoring Congressman by mentioning that I saw no representative of the newspaper industry on the schedule of witnesses in behalf of this legislation. To the best of my knowledge in a check with your most capable staff member who even found my way around this place yesterday, for which I thank her, there were no newspapers that supported it in any way. I think that would put some question into the statement that members of the opinion-molding industry are supporting the legislation, and remember that people who are going to get benefit of a legislative action have highly paid lobbyists to help state their case. Those who are opposed simply because they think the proposed legislation is wrong are not likely to be so active. Now when it comes to the theater industry and the greeting cards industry, I have a real lack of knowledge because I haven't thought about the be-alls and end-alls. I would say that I don't think it appropriate for my taxpayer money to be used to finance a skin flick on 14th Street, and I don't see how you can finance one theater and without getting into censorship if you deny the skin flick theater financing. Now I don't feel that skin flick theater should be banned the same way I don't think Hustler magazine should be banned. There is a difference between using the taxpayer's money to support something and letting people spend their own money to support it.

In testimony in support of this legislation, Steven Riekes claimed that the Small Business Administration can make its decisions on the basis of the credit-worthiness of a venture without looking at or without getting into the censorship question. In my opinion the political approach of a newspaper is often the key to the financial success of a publisher, and, therefore, to his credit worthiness. A newspaper which strongly opposed American support of Israel, I don't think could possibly be financially successful in the community of Pikesville, MD, or Bethesda or the New York area where it would just have no hope of being financially successful. Yet if the Small Business Administration were to ask a publisher now what is your feeling—I want to publish a paper in Pikesville, and I am anti-Israel, let's say, he's using political power or using improper influence on the press in my opinion. A newspaper which did not consider the interest of the black community should not really be successful in Mr. Mitchell's district in northwest Baltimore, neither would a publisher who espoused the interest of a black power in

Cicero, IL. Now a newspaper which has the reputation of being particularly conservative or particularly liberal at times can be at an advantage or at a disadvantage in getting paid circulation and in getting advertising.

We need look no further than right here in Washington at the Washington Times to see the validity of the point that the particular political approach and I guess what we would call the background of the ownership has a real influence on a newspaper's chance of financial success. I've spoken to a great many advertisers in this area trying to convince them of the obvious fact that they ought to be in our newspaper instead of wasting all their money in the Post, and the subject of the Washington Times often comes up. The feeling is universal. I don't care how much profit we would receive from our advertising in the Washington Times, but thanks to their ownership and thanks to the Moonies and the fact that they steal children and all these other allegations—I am not saying that they do, but there is a reputation for it, we wouldn't spend a penny in their paper. There are numerous people I know who absolutely despise the Washington Post, subscribe to it and would far prefer if you gave them a Washington Times, took the banner off and that would be a great paper. They wouldn't let it in their home because of the background of the ownership and in short, the political approach of that newspaper. In my opinion the Washington Times is a perfect example that it is impossible to forget about the political approach of a newspaper in order to determine whether or not it can be financially successful. In my opinion the Washington Times would never be a great moneymaker if it had different ownership but with the quality that it currently has, would at least be not a terrible money loser, wouldn't be hemorrhaging. It could probably do a lot better than the Washington Star was doing. I think I am somebody who is reasonably well informed about newspapers—what can sell. With the Times, because of the political approach, because of its ownership, the answer is no. If I have a lot of excess cash, which I don't, and if somebody were asking me would you make a loan to so-and-so to start a newspaper in place A, I would be most interested in the political approach, not trying to further what I feel is right or wrong, but just whether there would be a market for it, and whether that political approach would cause a problem. I've been associated with one newspaper, and I believe Mr. Roth is on the minority side here, and it was in a community, and I'd rather not mention the name of it, it was predominantly a Democratic community and the editor was a Republican, felt they should endorse every Republican. I said, well, I have no intention of participating with you unless at least a third of the people you endorse are Democrats. I don't care, you pick the third, but a community newspaper in this particular community, I don't believe can succeed if it is considered plainly a mouthpiece for the Republicans because there are too many—and vice versa. I don't think it would have succeeded—it might have succeeded as a mouthpiece of the Democrats, but in that particular community not to the Republicans. Again, opinion or the political approach of the paper, has an effect on its financial success.

Now there are always problems drawing a line—if you're having an opinion molder rule. We've heard, I think, Mr. Vandergriff

makes very pointed comments about movie theaters, and what is and what isn't. There is a question when you get toward that line and people—the Small Business Administration might be erring the wrong way. That is fine. Let's look at the minor problems, but let's not look at the basic rule. The San Diego Law Review was quoted as saying the Small Business Administration opposes the change in the rule, and it doesn't want to get involved in controversial issues. He claimed that the administration should not have as its goal avoiding embarrassment but should be assisting all legitimate small businesses. Our small business is different. We are assisted by the Government thanks to the first amendment, in fact to the very strict method—interpretations of that amendment the Supreme Court has issued. For instance, a town can't use its litter laws to prevent us from distributing a paper free of charge on everybody's lawn because of the first amendment rules. No other business would have that right.

Another reason for one of the Administrators of the Small Business Administration was indicating why this should be at least thought about was the tendency in the newspaper industry for the growth of the major chains. Another is the tendency for there to be but one metropolitan newspaper in almost all of our big cities. Mr. Theiste has said that he felt that the present opinion molder policy relative to the media industry eligibility may be unnecessarily inhibiting the Small Business Administration's ability to assist these small businesses. Now I run a small business which is safely in the black, and I am not worried about chains nor the Washington Post so long as we have strict enforcement and perhaps stricter enforcement than we now have of the antitrust laws. When I was the general manager of a paper in Alexandria called the Port Packet, we competed with a fairly goodsized chain, and in 2 years our weekly was in the black, and we carried more advertising once a week than the Alexandria Gazette, a daily then owned by that chain carried 5 days a week or 6 days a week. A small chain weekly, the Alexandria Journal had a significant loss in circulation, I think, because of the Port Packet. The reason for this success, in my opinion was that we were local. Our management was everywhere. The daily's was in South Carolina and the journal's was in Washington, not in Alexandria. One of the specific worries I do have though about major metropolitan newspapers is that the antitrust laws should prevent them from publishing shoppers total market coverage shoppers which they're prone to do where they take a loss. Now the Washington Post is not guilty of that but some major metropolitan newspapers are, in fact, some small city newspapers have to compete mildly with us.

Mr. IRELAND. Mr. Kennedy, can I get you to sum that up a little bit?

Mr. KENNEDY. OK. Well, this particular newspaper is giving away—if you buy a classified ad in the regular newspaper you get it free in the shopper, which is affecting us, and I think that that might have an antitrust problem. There are a lot of small newspapers growing up, and our business has been growing rapidly. I believe our industry does not need the type of help that this legislation would offer, and I think the passage of it would hurt the development in the small newspaper business. Any questions?

[Mr. Kennedy's prepared statement follows:]

PREPARED STATEMENT OF DAVIS LEE KENNEDY, PUBLISHER AND EDITOR,
GAITHERSBURG GAZETTE

I represent nobody other than myself and the publications I publish and edit. I would like to take this opportunity to thank you and the members of your committee for the opportunity to testify about the proposed legislation.

The Small Business Administration has testified over the years that it is opposed to any change in its so called "Opinion Molder Rule" based on two grounds, "the avoidance of the appearance of controlling or influencing the freedom of communication and the editorial selection of such communication material" and that it does not wish to be identified in any way with the opinions and ideas expressed by businesses with the capability to "mold opinion".

I think that both of these concerns are most justified and should be seriously considered by the House of Representatives and the members of this subcommittee while they consider whether or not to pass the legislation proposed by the Hon. Joseph Addabbo.

The press in this country is a most unusual business in that it enjoys a large number of privileges which are not available to the ordinary citizen or the ordinary business.

An example is that in the State of Maryland we are allowed to decline to identify our informants before the courts if in our opinion to do so would make it more difficult for us to report the news. No other business has a similar privilege. Ours is the only business specifically protected by the Constitution of the United States. We can place our products, unsolicited, on people's lawns and the municipal authorities according to the Supreme Court are not allowed to prohibit it under the anti-litter statutes. I could go on and on.

Suffice it to say that the press is not an ordinary business.

There is good reason for this protection. Governments the world over are often afraid of opinion. They also want to get across their version of the "unvarnished truth". This is as true in a small municipality as it is in Washington, DC. We need only remember the statements made by President Richard Nixon during the Watergate hearings to recognize that some governmental officials will go to just about any extent to see their version of the "truth" reaches the public.

The Small Business Administration is no exception. Just a few years ago a small weekly called The Washington Business Review published a series of stories about a purported scandal in the Administration. The Small Business Administration was, in my opinion, not completely forthright when it came to answering the charges.

The reason for this desire on the part of governments to influence or control the newspaper industry is that we, unlike most all other businesses, have the power to influence the opinions of the governed about their government.

The Small Business Administration has the statutory objective to aid, counsel, and assist the interest of small business concerns. It does not have the statutory objective of influencing the opinions of the governed about their government. I would commend the Administration for its recognition of its proper role via its "opinion molder" rule.

Some newspaper I have read are absolutely tasteless. Legally, they are probably not obscene thanks to the strict interpretation of The Supreme Court when it comes to a definition of the word obscene. I think it would be most improper for the government to give direct financial aid to businesses which the majority of our citizens consider obscene or morally offensive. I would certainly not say that this type of publication ought to be banned. But it is quite clear that we cannot and in my opinion we should not depend on the courts to prevent the taxpayers' money from being used to finance the startup of a magazine such as Hustler or a newspaper filled with hate propaganda.

The press is somewhat like the church. We need to be absolutely independent of the government if we are to remain free and true to our beliefs. That is why our Founding Fathers so wisely protected both press and church from governmental harassment with the First Amendment.

Would the Washington Business Review have been so pushy in its attempt to expose purported shenanigans of the Small Business Administration if it had been dependent upon the Administration for its financing. I doubt it. It is awfully difficult to call a governmental official a crook and then go to the same official for a loan extension.

In this case the conflict is obvious. But what if a newspaper were to accuse one of the members of this subcommittee of something untoward and this newspaper were

the recipient of a Small Business Administration loan. Would there not be a slight tendency upon the part of some future member of the committee who is not as up-standing as the present members to try to use a bit of influence to remove the financing or kill an extension? Would there not be fear on the part of the newspaper not to go ahead with the publication for fear of that influence? Would there not be fear that a member of the Congress would use his or her influence with the Small Business Administration to remove a loan?

Would there not be a tendency on the part of one of the less honorable members of the Congress to ask the Small Business Administration to help a newspaper which politically agreed with him or her? Would there not be a tendency on the part of a President such as Richard Nixon to try to force the Small Business Administration to finance a newspaper venture where the publisher would be supportive of that particular President?

Should a governmental agency receive the power to finance the media, there is no question but that same agency would have the power to destroy the media.

I think I have summarized the main reasons why this legislation should be rejected. Now, might I answer some of the points raised by its proponents.

The Hon. Mr. Addabbo has pointed out that the opinion molder rule has been ignored in cases where other agencies of the government regulate the media. This has allowed financial assistance to some opinion molding businesses.

The problems of this government assistance and regulation are obvious. Did not President Nixon threaten The Washington Post's television licenses thanks to that newspaper's Watergate coverage? The answer is to expand the rule's application.

The Hon. Mr. Addabbo has mentioned that affected small businesses engaged in the communication of ideas have strongly opposed the rule and criticized the administration's application of it. Might I answer by mentioning that I saw no representatives of the newspaper industry on the schedule of witnesses in behalf of this legislation. Might I add that if our industry favored this legislation, why did they not support it?

People who are going to get the benefit of a legislative action will hire highly paid lobbyists to help state their case. Those who are opposed simply because they think the proposed legislation is wrong are not likely to be so active.

When it comes to the theatre industry, and the effects of this rule on it, I must confess total ignorance. Whether or not the opinion molder rule is appropriate to theatres is a question I do not feel competent to address. However, as a taxpayer I would not wish to be forced to finance a skin flick that borders on the obscene.

In testimony in support of this legislation Mr. Steven Riekes claimed that the Small Business Administration can make its decisions on the basis of the credit-worthiness of a publishing venture can be examined without looking at the political approach of a particular publisher.

In my opinion the political approach might often be a key to the financial success of a publisher and therefore be a key to his credit-worthiness.

A newspaper which opposed America's support of Israel would probably have several strikes against it were it to be published in Pikesville or Bethesda, Maryland. A newspaper which did not consider the interests of the black community would not be too apt to be successful in Harlem. Neither would a publisher who espoused the interests of black power advocates in Cicero, Illinois.

A newspaper which has the reputation for being particularly conservative or particularly liberal can at times be at a disadvantage—or at an advantage—when it comes to its success in selling subscriptions and advertising.

We need look no further than The Washington Times to show the validity of this point.

I know numerous people who will not let that particular newspaper in their home thanks to its association with the so-called Unification Church or "the Moonies". I know of numerous advertisers who would not use it even if it were to prove profitable for them thanks to its association with "the Moonies". Many of these same people think that the paper itself is an outstanding one and they would prefer it to The Washington Post—if it were not for "the Moonies".

I would not be willing to make a loan to The Washington Times and I do not think it would be a good risk—because of its ownership and its policies. Before I would make a loan to any newspaper publisher, I would want to know of the political approach of that publisher. I would want to know if that approach would be likely to find a market. I am not saying that I would not make the loan if I disagreed with the political approach. I am just saying that I would want to consider the approach in making a judgment as to whether or not the publication might be successful.

Mr. Riekes claims that there is no "presumed prior restraint problem" because an opinion molder would fear a demand for early repayment if he "expresses a controversial opinion". He says this is not a legitimate fear because the Small Business Administration "may demand repayment of the loan only in the event of default".

Let me just say that from time to time I have owed my banker money. It is entirely possible that I might have technically defaulted for a minute or two on his requirement that I keep a certain level of compensating balances. It is very easy for a business to be technically in default on a loan and if the loanmaker wants to find some reason, it is often pretty easy. This is particularly the case of a small business where there is no financial vice president charged with seeing that no technical default ever occurs.

Mr. Riekes makes a large number of criticisms of the way the Small Business Administration interprets the rule on opinion molding. I might suggest that whenever a line is drawn on anything, one can often find some fine points where one could go one way or the other. The fact that fine tuning might well be needed does not in any way mean that the basic rule itself is inappropriate.

He also quotes the San Diego Law Review in claiming that the reason the Small Business Administration opposes change in the rule is that it does not want to be involved in controversial issues. He claims that the primary function of the administration "should not be to avoid embarrassment, but should be to assist all legitimate small businesses".

I guess I must simply say I disagree. Some small businesses, by the very nature, should not be the recipient of government or taxpayer funds. I think that it should not be the primary function of the Small Business Administration to finance businesses which either affect the opinion of the governed about government or are by their very nature offensive to a large number of taxpayers. One of the primary reasons for this proposed change in policies is the tendency for the newspaper industry to be run by big chain operators. Another is the tendency for there to be but one metropolitan newspaper in most of our big cities. Harold Theiste, as associate deputy administrator for the Administration has indicated that he is concerned that the "present opinion molder policy relative to media industry eligibility may be unnecessarily inhibiting our ability to assist these small businesses".

I run a small business, which is safely in the black. I am not worried about chains, nor by The Washington Post, so long as we have strict enforcement of the antitrust laws.

When I was the general manager of The Alexandria Port Packet, we competed with a good-sized chain. In two and a half years we turned the Port Packet into the black. We carried more advertising once a week than the chain newspaper did five days a week. A chain weekly, The Alexandria Journal, had a significant loss in circulation, in my opinion due to our success with The Port Packet.

The reason for this success in my opinion was that we were local. Our management was everywhere. The daily's was in South Carolina and the chain weekly's was in Washington.

I am not worried about competing with major metropolitan papers so long as the antitrust laws prevent them from publishing shoppers on which they take a loss. The Washington Post had advertising gains of about 2 percent last year. The Gaithersburg Gazette had a gain of 18 percent. We seem to be doing reasonably well.

Here in Washington we have a host of other small newspapers. In Montgomery County alone we directly compete with The Potomac Almanac, The County Express, The Sentinel, The Advertiser, The Montgomery Journal as well as of course, The Washington Post. The county also boasts several newspapers with which we do not directly compete including The (Poolesville) Bulletin and The Suburban Record.

Our industry gives every indication in this area of thriving. We are certainly not suffering because we cannot get direct loans from the Small Business Administration. So long as our competition does not benefit from Small Business Administration financing, we cannot claim that we are treated unfairly.

Indirectly, of course, we can get help from the Administration thanks to Small Business Investment Corporations. These venture capital firms have made loans to local area newspapers including The Washington Business Review and The Alexandria Port Packet. However, here no governmental official made the loan. An independent venture capitalist did. The risk and the reward is his, not the government's. And the potential for pressuring the editorial policy of the paper is with the private venturist, not an agency of the government of the United States.

If, in spite of the plethora of small newspaper businesses growing up both around and within many of our major cities, your committee wishes to give us assistance, we suggest you look carefully at postal rates for local newspapers, both paid and

free. Here one can give assistance in a truly neutral way for there is no element of judgement. Either the newspaper fits the category or it does not.

I believe that our industry does not need the type of help that the legislation currently on the table would offer. In fact, I believe the passage of this legislation would serve to hurt the development of the small newspaper business for it might leave some members of our industry in a position where they would fear they would have to kow-tow to elected officials or to government bureaucrats.

Thank you for your time.

Mr. IRELAND. Well, we really appreciate your taking the time to talk to us, and make your strong statement. Let me ask Mr. Vandergriff if he has questions.

Mr. VANDERGRIFF. Yes. I was interested in your comment about the major metropolitan papers. What about a lot of the published shoppers. Many of them are very competitive.

Mr. KENNEDY. Yes?

Mr. VANDERGRIFF. We've had a rash in my metropolitan area of shoppers being published, but not by the major metro newspapers.

Mr. KENNEDY. No problem.

Mr. VANDERGRIFF. You have no problem with that?

Mr. KENNEDY. The problem we have is—

Mr. VANDERGRIFF. You would be satisfied that SBA has talked about providing funding for shoppers before you?

Mr. KENNEDY. I would not like the SBA to be doing either, but I can think of no constitutional reason why it can't do a shopper. My concern about shoppers is when they are owned by the newspaper, the metropolitan newspaper, and they are subsidized by them. My personal opinion is that a newspaper, a well-run newspaper can overcome a well-run shopper, and we've done it in Gaithersburg.

Mr. VANDERGRIFF. Well, I know you have a good paper. My secretary lives in Gaithersburg, and she speaks highly of your paper. I want to insert that into the record.

Mr. KENNEDY. Thank you, sir. [Laughter.]

Mr. VANDERGRIFF. But let me ask you this. In my section of the country the small community newspaper, and I have about 100 cities, large, small, and in between in my district—many of the small town newspapers don't really have an editorial policy at all. They don't really publish editorials. That may or may not be true in this general section of the country, but I really find it difficult because I look at some of the small town papers, and some of them are really struggling. The community so desperately needs a paper. I don't really look upon them as opinion shapers. I am a layman. You're a professional in the field. Do you see any basis for my comment where small town newspapers are often concerned that they don't appear to be opinion shapers to me. They're publishing purely local news. Most of the small newspapers in my area don't even publish any national or international news.

Mr. KENNEDY. We don't. Well, opinion can be local as well as national and international. We don't have ward system, but the town council in Barnesville, MD, population 151, and we cover their meetings. We certainly mold opinion about those particular town council members. We're fussing with the school board right now in Montgomery County. We are certainly molding opinion about those elected officials in the Montgomery County School Board. We're certainly affecting opinion about how well the City Council of Gaithersburg is doing, and when it comes to the President of the

United States we have no influence. A Senator, very, very limited. Mr. Barnes, maybe a little bit, but when it comes to the mayor of Gaithersburg, we're certainly molding opinion.

Mr. VANDERGRIFF. You've seen the kind of small town newspaper I was talking about, however.

Mr. KENNEDY. Yes, sir.

Mr. VANDERGRIFF. Which I dare say is in a different realm altogether from even your paper.

Mr. KENNEDY. We have a very small paper in Mount Airy, which we also publish which would be similar to what you're talking about.

Mr. VANDERGRIFF. I see.

Mr. KENNEDY. I will just say that the mayor of Mount Airy was hot on the line to me because we'd published a story and indicated—they were having a cable TV franchise, and it wasn't—I don't want to get into the merits of it, but he was not too happy with the story. We were certainly molding opinion.

Mr. VANDERGRIFF. Well, I just couldn't help but harp back to your statement about some television programming that you wouldn't object to and see the SBA aiding—

Mr. KENNEDY. No, no, sir. I said I do not feel it appropriate for the SBA to aid it; however, I don't think it should be banned. Just because I don't think taxpayer funds should be used to finance something doesn't mean it should not be.

Mr. VANDERGRIFF. I see. Well, I appreciate your clarifying that. Thank you, Mr. Chairman.

Mr. IRELAND. Mr. Stenholm and Mr. Roth.

Mr. ROTH. Mr. Chairman, thank you. Mr. Kennedy, I appreciated your testimony. I think you made some very interesting arguments. The thing that I can't get out of my mind is this editor you worked for who endorsed all Republicans. Where is this man? [Laughter.]

Mr. KENNEDY. I didn't work for him. I was his partner. I'll forget about him.

Mr. ROTH. I hope he's still in the business, because I know newspaper editors as all Democrats but not all Republicans.

Mr. IRELAND. You have a bill for the appropriate—

Mr. ROTH. When I get around many people say, well, we have got freedom of the press in this country, but not for the people—for the people who own the newspapers. There's some truth in that, you know, because the people can't write their own editorials. Newspapers can.

Mr. KENNEDY. It is very easy to get into the newspaper business. There is a gentleman in our area who is one of our competitors. My guess is that he has a net of around \$10,000 invested. It is an industry for entry into the community—small newspaper business entry is very easy. You don't have to buy a press. You use somebody else's.

Mr. ROTH. Well, it's one thing to have a small newspaper. It is quite another to have the Washington Post. Not everybody can have the Washington Post.

Mr. KENNEDY. But the Washington Post can't get an SBA loan.

Mr. ROTH. Well, that's true. Thank you, Mr. Chairman.

Mr. IRELAND. Yes, indeed. Mr. Kennedy, we appreciate your comments.

Mr. KENNEDY. Thank you, sir.

Mr. IRELAND. Our next witness is Robert E. Park, professor of law at Georgetown University here in Washington. We're delighted to have you here. Mr. Park has been a teacher of administrative law since 1965 and constitutional law since 1971. We'll convene your testimony, and I want to thank you on behalf of the subcommittee for taking time to come and appear before us. I am quite aware, and I want the others to be aware that you used your own time and your own opinion molding techniques to present your testimony. We're delighted that you're here. I would ask you if you would, to summarize your testimony, and let us ask a few questions.

Mr. PARK. Thank you, Mr. Chairman. I would want to point out that I am from George Washington University not from Georgetown Law School.

Mr. IRELAND. Did I say Georgetown? I am sorry. That is a serious problem there because it is written George Washington, and I take full responsibility there, and I am sorry.

TESTIMONY OF ROBERT E. PARK, PROFESSOR OF LAW, GEORGE WASHINGTON UNIVERSITY

Mr. PARK. I appreciate this chance to appear. I think that the problem that you're working with is a very interesting problem and a very important problem. If I could just summarize my position, then I would be glad to respond to any questions that you might have.

I think we should start by reminding ourselves that the basic purpose of the loan program is to help small business. This is an economic purpose. The agency is primarily a business and financially oriented agency.

I think its competencies in the area of the first amendment are limited. It is a small aspect of their job, and the rule that the SBA has adopted, the opinion molder rule, is an attempt to make that administration easy, and, I think, constitutionally safe.

The rule raises two problems for your committee and for the Small Business Administration. First, you want to be fair to all small businesses, and I thought Mr. Vandergriff's questions about why can't we have a loan for a movie theater caught that notion of fairness very nicely. Second, this regulatory and subsidy activity takes place within a constitutional context that is extremely rigorous, that is very stringent in its requirements. In the first amendment area of free speech, things that look like a perfectly good common, sensical, and practical solution may turn out to be a nightmare in terms of administration.

I think that risk is inherent in the problem that you're addressing, and I hope that some of the things that I say will be helpful.

Nevertheless, I want to emphasize this sense of unfairness that people are going to have. I grew up in a small town, Mr. Vandergriff, very much like the towns you represent.

To tell a movie theater operator there that he was an opinion molder might flatter him, but it would more likely puzzle him. He

doesn't see himself as an opinion molder. He sees himself as offering a kind of merchandise. The fact that the movie industry, as such, has enormous opinion molding power is something that is just not visible to him. The first amendment is not very visible to him either. I think if you look at the comments that businessmen and agency administrators make, they don't show the kind of sensitivity to the first amendment that two groups of people in this country show. One group is the Supreme Court and the whole legal establishment. They are very sensitive to the first amendment. The other group is the press.

I thought Mr. Kennedy's comments were extraordinarily sensitive to first amendment values. I just can't say too plainly that to understand the problem you need to understand that perspective. The way Mr. Kennedy presented it is, I think, very much the way the courts perceive it. Now on the central issues I was asked to address: Is the present opinion molder rule constitutional? And, is H.R. 1157 constitutional?

I have reviewed the SBA's Opinion Digests. I have looked at the comments that were given at your hearing in November, and I have looked at some cases that deal with related types of regulation. There's only one case to my knowledge that deals with the opinion molder rule immediately, and that is the *Lorcher* case. However, the Internal Revenue Service regulations, in section 501(c)(3), afford tax exemptions for educational and charitable institutions, and face a similar kind of problem. That is to say that for organizations engaged in propaganda or public interest advocacy, the IRS has had to set standards for qualifying for the tax exemption. They've done it by requiring full and fair treatment of controversial topics in the publication. Otherwise, the organization does not qualify. This has proven difficult to administer, and constitutionally controversial, with cases going in different directions. But, on balance, in the tax area, as in the spending area with which we're dealing with the SBA rule, we have seen the courts deferring to the Government's discretion as long as there's a rational basis for it. The SBA loans and the IRS tax exemptions are not areas in which you must demonstrate a compelling necessity to have a constitutional regulation of some aspects of speech. The compelling necessity requirement arises where you are negatively impinging on first amendment freedoms, not when you are deciding how to spend your own money. When Congress decides what it will spend, it is not thereby silencing a voice for those organizations or activities that it does not assist. A case from the last term of the Supreme Court was very emphatic on that point. *Regan v. Taxation with Representation*, 76 L Ed 2d 129 (1983). This case is, I think, a very good guideline as to the law in this particular area. Now as to the constitutionality of the SBA regulations, I would review them in the context of the congressional intent. That ought to be the focal point: What is it that Congress wants? Congress made a broad delegation to the SBA to administer the loan program in the public interest. That is a very open ended delegation. We have the problem, though, that this broad delegation comes up against first amendment rights. So we have to ask not only what did Congress want to do, but can it be done constitutionally?

Does the SBA correctly interpret the congressional intent. I think, as I understand what the SBA is trying to do, that the SBA does correctly understand the intent of Congress, and I think it was wise of Congress to give a public interest content to the delegation.

Now what is it that the SBA thinks that the Congress wants. It seems to me, if I read the SBA position correctly, that the SBA understands Congress as wanting the SBA to be careful not to subsidize businesses that are not in the public interest and not to infringe upon constitutional rights, that is, to insulate first amendment advocates from SBA influence, either in terms of specific content review or in terms of an inducement to get a loan or to have a loan renewed. The SBA might also improperly influence an "opinion molder" by other administrative actions, such as deciding to extend a loan for additional time, or to modify its terms when a default is pending.

I think the SBA has presumed that Congress would not want tax money to be loaned to make possible a propaganda sheet of some kind, or to finance a propaganda publisher who has a controversial viewpoint, particularly one disfavored by the public. It seems to me, too, that those viewpoints should stand on their own feet or they should fail, and they should not be assisted with, Government tax money. I think that is the intent of Congress that the SBA has inferred from this broad delegation. I think most people would be inclined to agree with the SBA that Congress does not intend for tax money to be spent to establish a pornographic publisher or pornographic moviemaker or someone who is making pornographic video tapes. I think taxpayers would be quite concerned to know that the capitalization of such businesses came out of a Government loan. As Mr. Kennedy repeatedly said, no one here is saying that those people should not be free to make those kinds of movies. Short of obscenity, short of illegality, they have a constitutional right to do so. The question is whether Congress wants to spend tax money to support that kind of enterprise.

Now it seems to me important that the SBA has understood Congress, and the public interest criteria, to suggest that the SBA should not associate itself with political arguments. That is to say that people should not think that a particular position, a controversial position, is in some sense a reflection of Government policy because the Government is supporting it with tax money through low-interest subsidy loans.

Now the problem is, how do you design a regulation that achieves these public interest goals, but at the same time does not review what the publisher or what the moviemaker or the movie theater is doing in terms of its content? What is to be published is clearly for the business to say, not the SBA. It doesn't matter, as the Supreme Court said in *Taxation with Representation*, that subsidy powers are broad. The courts leave the decision as to who is to be subsidized to the discretion of the legislature and its agencies. It does matter constitutionally, though, if the legislature or agencies in any way, negatively impinge upon speech. When they begin to use criteria for loans or subsidies that are focused upon specific content, it seems to me that they're right at the edge, and I think over the edge, of an unconstitutional influence on free speech.

This rule, the "opinion molder" rule, thus, presents a practical problem. The problem is that the SBA is a business agency. It is not a first amendment expert in terms of framing policy. With all respect to my friends at the SBA, the first amendment is not their primary focus. Even if it were, first amendment analysis is extremely difficult to do successfully.

Now, for example, we see some areas where the Government is effectively overseeing content, but these are very narrow. We see it in the area of the FTC and advertising, one of the areas that the SBA has withdrawn from its own jurisdiction. The SBA has deferred to the Federal Trade Commission. At the FTC the focus is upon fraud, upon unprotected commercial speech, so the constitutional problems are minimized. We see it, also, in regard to the SBA deference to the FCC. The FCC regulates an area of speech in which the Government owns the medium, the air waves. When the Government speaks both as regulator and as a proprietor or when the Government speaks to regulate speech on its own possessions, as in the case of a military base, it has much broader power over regulating speech.

The Supreme Court in the *Pacifica* case said that in the broadcasting industry the FCC could regulate indecent speech. By contrast, state legislatures that tried to regulate merely indecent speech would threaten first amendment values, and would probably lose. But the FCC represents a peculiar situation.

Now it does not matter to the SBA that the FTC or the FCC has not chosen to regulate more aggressively. Those are their jurisdictions. Those are their responsibilities. The SBA is rid of the burden of regulating speech as to matters within FTC and FCC jurisdiction, and frankly, I am more comfortable, for example, with the FCC regulating broadcasting than I would be with the SBA doing it.

The FCC is intimately involved with a media establishment. It is much more sensitive to what it is doing, and necessarily so.

On the opinion molder rule it comes down in my mind to this. You've got to have categorical rules in this area, but not one that throws out the baby with the bath. As I try to suggest in my statement, a regulation should not affront common sense, and people who are not pornographers resent being lumped together with them and disqualified. But it is very difficult to make a rule that will survive a first amendment attack.

That some of the rules suggested by the SBA are workable, but it seems to me that some of them clearly affront the prohibition against content review. These would not survive judicial review. On the other hand, it seems to me there are ways even under the present regulation to narrow it satisfactorily so as to broaden eligibility. I think the SBA could focus upon a content neutral process rule, for example to designate movie theaters, for example, in terms of whether or not they are promoting or advocating a viewpoint.

Even the single film movie house, if it did not promote or advocate a viewpoint, which is the present SBA exception for the general book store, could be made eligible. I don't think it would violate equal protection, and I think it would serve the purpose of broadening the class of loan eligible firms. But as soon as you see a trend

in movie scheduling, that is, when you detect, as a matter of fact, that the theater is becoming a promoter or advocate of particular viewpoints, that promotion of a theme or viewpoint would be disqualifying.

So it seems to me that these objectives of the SBA and of those who wish to broaden loan eligibility might be reconciled. But it is a very difficult area.

I think what has happened to this point is that the Small Business Administration has drawn a prudent, relatively efficient and constitutional rule that keeps it as much as possible out of the business of reviewing these businesses' opinions.

As to H.R. 1157, I think that this is a very difficult bill to work with. Let me just make several points quickly. When Congress names the businesses that are to be taken out from under the opinion molder rule, as in H.R. 1157, it does more than simply categorically accept them. It seems to me that it says to the courts and to the public that as to these types of businesses there are no residual public interest criteria for the SBA to apply. I would read adoption of H.R. 1157 as saying, in effect, "stay away from these businesses and give them the loans, unless you can do some kind of a review through 'legitimate public interest.'" Legitimate public interest, which is the language of H.R. 1157, is a Trojan horse. I think it will be struck down as unconstitutionally vague. I think it is impossible to make sense out of it. The friends of the bill who spoke in favor of it, said that they couldn't understand what legitimate public interest meant, and I don't think anyone, not even a fairly sophisticated lawyer, can tell you what the difference is between the public interest and the legitimate public interest. I think what a court would have to do is to decide, since "legitimate public interest" is in the statute, what content it was intended to have. Congress does not draft idly. A word is presumed to be in a statute for a purpose. Does it mean, in fact, that "legitimate" for these named businesses cannot refer to the nature of the business?

I think that would be a natural reading. Does it mean, in effect, that there is an inference that the opinion molder rule is not a legitimate public interest, since H.R. 1157 is clearly attacking the opinion molder rule. It seems to me that that is a perfectly natural inference to draw. I think it is a very destructive phrase in the bill.

Now not only is it impossible to give meaning, I think, to "legitimate public interest," but as soon as the agency tries to give meaning by adopting regulations, they're going to be in violation of the first amendment because the regulations will not be content neutral.

Legitimate public interest has got to have added a practice regulation, rather than a topical definition like "pornographic bookstores." I think that any attempt to say that it is not in the public interest to fund with Government money pornographic bookstores, although we all would agree that it is true, would be struck down as unconstitutional as soon as it was put in the hands of the court. Now perhaps the SBA could have some success in drafting process rules. I don't know. It would be difficult because the Congress in adopting H.R. 1157 will have so undercut the notion of public interest that the kinds of SBA rules that could then be adopted, constitutionally, could be very difficult to frame.

Now it does seem to me possible that the Congress could set standards, itself, but I just suggest to you that if you think about legislating in the area of indecency, for example, what a nightmare that is going to be, and how much litigation you're going to draw.

Let me give another aspect of the H.R. 1157 problem, "legitimate public interest." Let's assume for the sake of argument that we think obscene movies would be a proper category for loan exclusion. If that were the standard, and you then tried to apply it to obscene movies, using the illegality standard, what is the SBA going to do? In *Miller v. California* the Supreme Court said that every jurisdiction in the United States could define its own standard as to obscenity. Is the SBA here in Washington supposed to define rules that comprehend 50 different territorial definitions of obscenity? It boggles the mind. It can't be done. And the question remains as to whether or not national obscenity standards, which is an alternative to the *Miller v. California* holding are workable. If the hypothetical national standard is "higher", that is, less tolerant of speech than the local standard, can the local standard be a constitutional basis for attacking the SBA statute or SBA regulations? We don't even know. We don't have case law. To invite the SBA to regulate in this area, it seems to me just invites folly. First amendment regulation is not their expertise, and they're going to be subjected to endless litigation.

Well, that is it. If I can be of any help in answering questions, I'd be pleased to try.

[Mr. Park's prepared statement follows:]

PREPARED STATEMENT OF ROBERT E. PARK, PROFESSOR OF LAW, GEORGE WASHINGTON UNIVERSITY

Mr. Chairman, I am Robert E. Park, Professor of Law at The George Washington University of Washington, D.C. I appear in response to your invitation to comment upon the Small Business Administration's "opinion molder" policy and upon H.R. 1157. The "opinion molder" rule and H.R. 1157, which would eliminate the "opinion molder" rule, are of special interest to me as a teacher of administrative law, which I have taught since 1965, and of constitutional law, which I have taught since 1971. My opinions are my own, or course, and are not offered to represent in any way the views or policies of The George Washington University or its National Law Center. Thank you for this opportunity to appear.

SUMMARY OF CONCLUSIONS

1. The "opinion molder" rule is constitutional, and a prudent agency policy in light of the Small Business Administration's business and financial orientation and limited First Amendment expertise.

It is my opinion that the "opinion molder" policy of the Small Business Administration, as expressed in 13 CFR 120.2(d)(4), is constitutional. The policy has been adopted by the SBA as a means of promoting First Amendment values. It insulates First Amendment enterprises from the risk or pressures of SBA content review by categorically rejecting them from consideration for SBA loans. The "opinion molder" policy is a long established one, but, over the years, SBA's application of the "opinion molder" policy has not been a model of clarity, consistency or constitutional sensitivity. I would infer from the agency's track record that SBA's competencies are primarily those of business and finance, and not First Amendment theory. Thus, SBA's attempt to devise a simple, clear test to insulate First Amendment enterprises from regulatory intrusion may well be a prudent policy. The "opinion molder" rule has been narrowed and made more specific in recent years in response to congressional recommendations and, in one instance, judicial review. My review of the SBA Opinion Digest reports of cases decided in recent years under 120.2(d)(4) has persuaded me that the agency is attempting to apply the rule in a uniform, fair and realistic way to avoid any appearance of SBA encouragement or discouragement of particular ideas or opinions. Although the SBA policy of maximizing the separation of "opinion" enterprises from SBA loan administration is constitutional-

ly permitted, it is not constitutionally compelled. Alternative policies could be devised to protect the First Amendment values in issue and also permit the SBA to afford financial support to some of the "opinion molder" firms. H.R. 1157 has been offered as such an alternative. It seems clear, however, that some of these alternative policies would be far more difficult for the SBA to administer. It also seems clear that some of these alternative policies, H.R. 1157 is one example, would almost certainly lead to the contraction or abandonment of that range of public interest values that the SBA now seeks to promote under its congressional mandate. For example, the SBA understands its public interest mandate from Congress to require it to avoid extending low interest government loans to "adult" bookstores, to sexually oriented movie theaters, to gambling enterprises, to racist newspapers, and to similar enterprises. The SBA understands its public interest mandate to require it to avoid identifying the government with particular opinions or viewpoints. The SBA understands its public interest mandate to require it to avoid any relationship with First Amendment enterprises that might induce them to tailor their views in the hope of obtaining an SBA loan. It is my conclusion that the "opinion molder" policy does promote First Amendment values and the other public interest values identified by the SBA. Other policies might promote other aspects of First Amendment values, and other aspects of the public interest, but the SBA policy clearly has a rational basis. The "opinion molder" policy has proven a relatively effective way for the SBA to avoid entangling itself in subtle controversies over First Amendment law. Given the largely business and financial orientation of the agency, the SBA policy of trying to avoid involving itself in First Amendment conflicts and line drawing may be its most prudent strategy.

2. H.R. 1157 would substantially complicate SBA loan administration and would jeopardize the public interest values now being promoted by the SBA.

As to H.R. 1157, it would require the SBA to abandon its policy of a strong separation of agency lending discretion from First Amendment enterprises. Instead, H.R. 1157 would require the SBA to make individualized determinations as to "the public interest" among "opinion molders." Trying to apply the public interest objectives of the SBA, as it has understood that congressional mandate, would be much more difficult on a case by case basis than by categorical disposition. First, it would be much more costly. Second, and more critically, it would draw the agency perilously close to content review of the particular opinions or activities of the loan applicant. The First Amendment risks are much more heightened in applications of public interest tests of decency, fairness of presentation, accuracy of information, etc., to the behavior of the firm than when the agency applies a content neutral categorical rule that excludes opinion makers as a class. The "opinion molders" rule is an example of the latter, of course. But under H.R. 1157 constitutional questions of equal protection, vagueness, overbreadth, the free speech clause, and the freedom of the press would be raised to challenge the "legitimacy" of SBA asserted "public interest." Either the SBA would have to abandon or dilute its conception of the public interest, or disputes over application of the standards would become a chronic problem. It is my belief that if H.R. 1157 becomes law and the SBA continues to attempt to administer loans by its understanding of the congressionally implied public interest standards of the past, the agency will become involved in constitutional litigation frequently and will be diverted from its principal business and financial responsibilities.

3. The Constitution affords Congress, and agencies under congressional delegations, very broad discretion in the exercise of the spending and taxing powers.

Finally, it is my opinion that some of the First Amendment criticism of the "opinion molder" rule misunderstands the controlling First Amendment standards. In a 9-0 decision of the last term the U.S. Supreme Court clarified this area of constitutional law. A public interest nonprofit corporation challenged a tax exemption regulation that disqualified those who engaged in substantial lobbying. As to the argument that denial of the exemption violated First Amendment rights, the Supreme Court unanimously held, "We again reject the notion that First Amendment rights are somehow not fully realized unless they are subsidized by the State." *Regan v. Taxation With Representation*, 76 L ED 2d 129, 137 (1983). As to the argument that giving the tax exemption to veterans' organizations who engage in lobbying while denying it to others violated equal protection, the Supreme Court unanimously relied upon this language from a 1940 opinion rejecting a similar equal protection argument in regard to a tax burden that fell differently upon different persons, "... the presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons and classes." *HARRIS v. McRAE*, 448 US 297, 322 (1940). Finally as to how sensitive the judicial review is to be "when Congress subsidizes some

speech, but not all speech," the Supreme Court rejected the Court of Appeals conclusion that strict scrutiny was to apply. "That is not the law," the Court wrote, and continued, later in its opinion, "We have held in several contexts that a legislature's decision not to subsidize the exercise of a fundamental right does not infringe the right, and thus is not subject to strict scrutiny. . . . The reasoning of these decisions is simple: 'although government may not place obstacles in the path of a (person's) exercise of . . . freedom of (speech), it need not remove those not of its own creation.'" At page 139, quoting *Harris*, above, at 316. This case, *Regan v. Taxation With Representation*, cited above, was decided 9-0 in support of an IRS regulation that is strongly analogous to the "opinion molder" rule. The Taxation with Representation decision would appear dispositive of many of the constitutionality issues made in opposition to the "opinion molder" rule.

PART I—DISCUSSION OF THE SBA "OPINION MOLDER" REGULATIONS

101. Does the SBA "opinion molder" regulation threaten First Amendment values?

The SBA is charged by Congress with administering the small business loan program in the public interest. This is a delegation of broad policy discretion. It is out of this broad discretion, rather than from any explicit statutory direction from Congress, that the SBA has fashioned the "opinion molder" policy. Given this broad "public interest" discretion in the SBA, it is certainly plausible that small magazines, newspapers and other First Amendment enterprises seeking loans might edit their speech to conform to the perceived preferences of the SBA. The SBA seeks to avoid this risk by insulating the First Amendment enterprises from SBA review at all. By regulation, SBA simply excludes "opinion molders" from loan eligibility.

This SBA policy is perceived by many as throwing out the baby with the bath, since the "opinion molders" are completely cut off from the loan program. Some alternatives will be discussed below. At this point we are inquiring into the constitutionality of such a policy. Under the reasoning of *Regan v. Taxation With Representation*, 76 L Ed 2d 129 (1983), a recent and analogous tax regulation case where the organization was denied a tax exemption because of its lobbying, the "opinion molder" rule would appear to be constitutional. The First Amendment, in itself, does not establish an entitlement to a government tax exemption, loan or subsidy.

An unconstitutional threat to First Amendment values would arise were the SBA to attempt to use its broad discretion to deliberately deny or control the First Amendment exercises of loan applicants. But a voice is not silenced merely because the government elects to subsidize another voice. The "opinion molder" rule does not violate equal protection merely because it permits loans to some and not to others.

Finally, absent an actual interference with the exercise of a fundamental right like freedom of speech, the standard for judicial review is that the legislation or regulation must have a rational relation to a legitimate governmental purpose. The language of strict scrutiny and of compelling necessity, often associated with First Amendment rights, is not applicable in the ordinary case of government subsidies, and does not apply to the "opinion molder" rule.

102. Is there a rational basis for the "opinion molder" rule?

There are several rational bases for the adoption of the "opinion molder" rule by the SBA.

First, although the Constitution does not compel the SBA to adopt the "opinion molder" rule, it is a legitimate purpose for the agency to seek to insulate loan applicants from any undue influence over their First Amendment rights, including the risk that the prospects of a loan may induce the "opinion molder" to conform to agency content preferences. That the loan applicants would prefer not to be so protected, and would rather have the cash, so to speak, is not controlling.

Second, the agency does not wish to be associated in the public or congressional mind with the controversies that accompany the vigorous assertion of First Amendment rights. There appear to be several rational bases for this agency preference: (1) The agency does not wish to lend the aura of government approval or support to ideas or publishers who are beyond the control of the agency. (2) The agency does not wish to disadvantage those persons who oppose the ideas in question, and who might feel that the agency support for their opponents puts them in the posture of appearing opposed to the government. (3) The SBA must be sensitive to the political consequences in Congress of the agency's being seen as having endorsed unpopular or highly controversial publications or media firms, e.g., a smut producing motion picture firm, an adult bookstore or a racist newspaper. (4) The agency does not wish

to have a loan disapproval perceived as a disapproval or attempt to suppress the ideas of the loan applicant.

Third, the SBA is a business agency. It has little expertise in weighing political values as they balance the loan program against First Amendment claims. The agency has no specific "public interest" statutory standards from which to derive operating regulations or policies. The SBA's past confusion and difficulties in dealing with such problems as motion picture theaters and with "generalist" versus "specialist" bookstores show how difficult it is for the agency to write plausible rules separating "content indifferent" business firms from the "opinion molder" business firms, to whom content is important. Further, deciding how to award loans to serve "the public interest" as between one "opinion molder" and another is substantially more difficult than the categorical exclusions the SBA has been employing. If one whole category of controversial loan applicants is disqualified, the problem is simplified. Further, if the remaining category has no significant First Amendment dimension to its loan applications, the review of the application can be made on business, financial and public interest grounds in a fairly direct manner. Thus, making subtle First Amendment distinctions is a task for which the SBA has little expertise, and very little appetite.

Fourth, requiring the agency to make particularized decisions on the record as to the public interest consequences of giving loans to "opinion molders" would be very complicated, would almost certainly generate frequent litigation, and would divert the agency's attention from its business skills and competencies. The costs, delays and administrative burden afford a rational basis for the SBA's reliance upon categorical exclusions.

Fifth, the "opinion molders" rule, and its predecessors, constitute a long standing federal policy. In spite of several opportunities, Congress has not chosen to overturn it. It is plausible to infer that Congress has found the exclusion of the "opinion molders" consistent with its broader economic and social purposes for the statute and the agency.

Sixth, if the SBA is required to administer a loan program to "opinion molder" firms, it is very possible that "the public interest" tests would collapse into mere financial criteria. Let's see how that might happen. The agency believes that Congress, implicitly in its statutorily imposed public interest criterion, does not wish to give loans to activities that many people believe are socially marginal or undesirable enterprises, such as adult bookstores, smut publishers and hate newspapers; nor to politically controversial enterprises, such as partisan journals and propaganda film makers. If the agency seeks to apply those public interest preferences on a case by case basis, it is very likely to encounter endless litigation and constant problems of judicial review. If the agency seeks to apply those public interest preferences by rule, it will find the rules extremely difficult to write and subject to similar litigious attacks. The result may well be that the agency will abandon these public interest criteria and make its decisions almost exclusively on the basis of business and financial criteria.

It appears that Congress has three options. First, Congress may choose to leave the regulation in place and continue to monitor the SBA's administration of the program. Second, Congress may choose to provide the agency with the detailed statutory guidance necessary to tailor the loan policy to a more precise administration. If this is its choice, Congress, too, will face many of the same difficulties of the narrow and precise drafting required in the First Amendment area, and similar prospects of extended attack in the courts. Third, Congress may push the agency into more particularistic, individualized adjudication under the general standard of "the public interest," which H.R. 1157 appears to seek. This third option moves the constitutional controversies to the SBA's adjudicatory process, and runs the risk of the abandonment of the public interest criteria, as noted earlier.

103. How are the "opinion molders" injured?

When inquiring into the question as to whether or not the government is using a subsidy to discriminate invidiously against particular disfavored ideas or speakers, one must ask in what way the subsidy has injured these speakers.

The Supreme Court made it clear twenty-five years ago that the failure of the government to subsidize First Amendment rights is not the same as a denial or suppression of such rights. *Cammarano v. United States*, 358 US 498 (1959). So this cannot be the basis of the injury.

The firms with whom the "opinion molders" compete, i.e., those within the same market sector, are also excluded from SBA loans. This suggests that there is only a limited economic or market disadvantage.

It may be worth noting here, again, that there is no equal protection right to a loan merely because Congress has afforded loans to a business of another type.

Broad constitutional discretion in the taxing and spending powers lies with the legislative branch, and rationally based classifications in this area do not generally offend equal protection.

Of course, the "opinion molder" firms would like the low cost loans and the profits therefrom, but there is no constitutional right to government subsidies.

Finally, since there is no right to government subsidies in general, the only remaining issue must be, "Is there a statutorily based right to a subsidy in the present instance that is being frustrated by the regulations of the SBA?" This would seem most unlikely, since Congress has been aware of the exclusion of "opinion molders" since the policy was originally adopted by the Reconstruction Finance Corporation, and has not acted to override it. Indeed, upon reviewing the agency's unsatisfactorily vague regulations in 1976, the Subcommittee on Small Business Administration Oversight and Minority Enterprise used that occasion to recommend to the SBA that it strengthen its regulations. The language of that Subcommittee Report clearly suggests that the Subcommittee believed the broad regulatory delegation from Congress empowered the SBA to disapprove loans to firms seeking to promulgate ideas and values inconsistent with that delegation. H.R. REP. NO. 840, 94th Cong., 2d Sess. 28 (1976).

In the light of the history of the "opinion molder" policy, it is difficult to conclude that the broad delegation of "public interest" powers to the SBA did not include the power to frame this policy. The "opinion molder" policy does not inhibit the broadest possible reach of the small business loan program, but since it appears to serve administrative convenience and to complement First Amendment values, and since Congress has been aware of it for many years and has not acted to change it, then this regulatory constriction as to who is eligible for a loan appears to be no more than a proper exercise of the rulemaking power of the SBA, pursuant to its statutory authority. If that is correct, the "opinion molder" firms have suffered no legal injury.

To sum up: The "opinion molders" do not appear to have suffered any deprivation of constitutional rights or other legal injury. The "opinion molders" have no right to a government loan or other subsidy, absent that created by Congress. The "opinion molder" policy does not appear to violate equal protection rights. Lost potential profits that the "opinion molder" firms would have enjoyed had they been given loans cannot be said to constitute an injury. There was no right to any such profits, absent Congressional provision for the loans. Since Congress has not disturbed the SBA's long-standing policy of excluding "opinion molders" from consideration, it is difficult to believe Congress has a clear intent that "opinion molders" had to be included in the loan program.

104. Is there a valid equal protection argument against the "opinion molder" rule?

As has been suggested, there is no denial of equal protection. None of the "opinion molder" firms are afforded loans except those situated so as to be subject to the regulation of federal agencies of appropriate competency, i.e., advertising is subject to FTC regulation and broadcasting is subject to FCC regulation. This limited distinction within the broad "opinion molder" class has a rational justification in the specialized competency and jurisdiction of the subject matter agencies. It does not matter that those agencies may have elected not to oversee the substantive content of the "opinion molders" within their jurisdiction. Those agencies are in a position to assess such matters and are responsible for them. As between the "opinion molder" firms and the content indifferent firms, a rational distinction was developed in Sec. 102, above.

105. Is the present form of the "opinion molder" rule unlawfully vague?

Vagueness in a regulation may be unlawfully offensive in four ways. (1) A regulation establishing entitlements may be so vague that the administrator enjoys unreasonable discretion to discriminate. This is particularly dangerous to fundamental rights, such as freedom of speech. (2) The regulation may be so vague that it fails to give fair notice of conduct that is prohibited or required, resulting in unfair penalties or denials of entitlement. (3) The regulation may be so vague that it makes uniform and consistent enforcement impossible. (4) The regulation may be so vague that it fails to afford reviewing courts a meaningful standard by which to adjudge agency conduct.

The current revised version of the "opinion molder" rule excludes from loan eligibility enterprises involving "the creation, origination, expression, dissemination, propagation, or distribution of ideas, values, thoughts, opinions or similar intellectual property, regardless of medium, form, or content." 13 C.F.R. 120.2d(d)(4). This classification divides loan applicants into two categories, those who are indifferent to the intellectual or value content of their enterprises, and those to whom the in-

tellectual or value content of their enterprises is important, though to varying degrees. Are the categories reliable and distinct? Are the criteria too vague to sort loan applicants reliably? Although hard cases arise readily, there does appear to be a principled basis for the distinction.

An illustration of SBA practice may make the "opinion molder" distinction more intelligible, and may show why it is difficult to understand and to apply. A general bookstore is prepared to sell whatever books people choose to buy. To such a firm, books are essentially merchandise, not messages of systematic or partisan importance. The SBA regards such a bookstore as loan eligible. By way of contrast, specialist bookstores, such as feminist bookstores, religious bookstores, "adult" bookstores, and similar enterprises, are not indifferent to the books they carry, but select them for their ideological, political, philosophical or topical content. The principle appears to be more than a test of specialization. It appears to be whether the bookstore itself appears to take an "advocacy" position. Indeed the regulation reads, "Specialty stores primarily selling products that promote or advocate ideas. . . ." 13 C.F.R. 120.2(d)(4)(vii). It is not an easy distinction to make, but it does appear to be a viable one.

Of course, problems abound. Suppose a bookstore specializes in medical texts, manuals, research monographs and related books. Within medicine there are numerous areas of intense controversy, many of them involving sensitive political, religious, ethical and social values. Is a book on counselling potential abortion patients likely to be content indifferent? A book on the psychotherapist's responsibility to child molesters? A book on public health responses to the acquired immune deficiency syndrome (AIDS)? A book on the right to die? Of course books on these topics are likely to assert controversial opinions, and are likely, often, to present them in a biased manner. The agency test of "promote or advocate ideas," therefore, obviously cannot be applied to the books themselves, anymore than it is in the case of the general bookstore (which may, of course, be selling some of these books). The proper test must be the purpose for which the specialist bookstore is organized. If the medical bookstore stocks a broad array of books, based upon demand rather than upon their ideological position, it should be seen as a specialized bookstore, but not as an "advocacy bookstore." The term "advocacy bookstore" catches the apparent intent of the SBA regulation's language of "promote or advocate ideas" more faithfully than does the term "specialist bookstore." 13 C.F.R. 120.2(d)(4)(vii).

To make the point more precisely, the real key to the bookstore dilemma would appear to lie not in whether or not the books are specialized by topic, but in whether the bookseller is engaged in "primarily selling products that promote or advocate ideas." 120.2(d)(4)(vii). In a phrase, "is it an advocacy enterprise?" It is not clear, however, that this principled implication of the bookstore subsection is seen by the SBA as pervading the "opinion molder" rule.

Incidentally, the SBA's policy of avoiding subsidies to firms that "promote and advocate" a particular viewpoint is paralleled by the Internal Revenue Service's regulation 501(c)(3). Since that regulation has been litigated on questions of equal protection, due process and infringement of First Amendment rights, it may afford a useful perspective of the "opinion molder" rule of the SBA. This parallel is noted in Part III of this statement.

PART II—DISCUSSION OF THE AMENDMENTS PROPOSED IN H.R. 1157

201. H.R. 1157 would require the SBA to make loans now denied, perhaps implicitly changing the meaning of "the public interest" under the Small Business Act.

It has been the SBA interpretation of Section 4(d) of the Small Business Act that "the public interest" mandate charged the agency with the evaluation of loan applications beyond financial criteria. Thus, the SBA has given weight to First Amendment considerations, seeking to avoid any chilling effect on speech. The SBA has also sought to avoid any appearance of a government endorsement of particular views, philosophies or opinions. Still further, it has been the SBA interpretation of the congressional mandate that to administer the program in "the public interest" required the avoidance of subsidizing with federal loans certain types of activities, such as "pornographic motion picture theatres and book stores, and those that deal in political, racial and pornographic greeting cards." Quotation attributed to Mr. Charles R. Hertzberg, then Deputy Associate Administrator for Financial Assistance, in a letter from Mr. Steven J. Riekes, Sept. 17, 1982, appended to his testimony to this Subcommittee on November 15, 1983.

However, H.R. 1157 may have the effect of changing the implications of this congressional "public interest" mandate.

H.R. 1157 would prohibit the Small Business Administration from applying its "opinion molder" rule to exclude from loan eligibility certain categories of named businesses. This is clearly within the power of Congress. But, the striking of the "opinion molder" rule may imply to the SBA, the public and the courts that the policies behind that rule are no longer part of the congressional "public interest" mandate to the SBA.

This implication is not contradicted by section (d)(2) of H.R. 1157, which presents special problems of its own. These additional problems are discussed below.

202. How H.R. 1157 might change the way SBA considers loans.

To illustrate how the "opinion molder" rule works now, and what its elimination might produce, let us look at a recent case of the SBA that is likely to become more common. In 1983 the SBA ruled that a home computer software company was ineligible under the "opinion molder" rule. The programs offered by the applicant included methods of keeping inventories and balancing checkbooks as well as developing video games. The SBA reported in its Opinion Digest, "Applicant is not eligible because it is engaged in the creation and dissemination of ideas and values." 124 SBA O.D. 114 (1983). This is a fairly typical application of the "opinion molder" rule, though a novel set of facts.

If H.R. 1157 becomes law, the software publisher will appear to be analogous to other publishers, and can no longer be excluded from eligibility solely because of the nature of its business.

Special situations arise. (1) Suppose the software game is racist? A software game, *Custer's Revenge*, was recently marketed that visually displayed in crude graphics General Custer raping an Indian maiden. (2) Suppose the software game is sexually oriented? A variety of home computer magazines display ads for sexually oriented software. (3) Recent developments have suggested that computers may have substantial power and efficacy as psychotherapeutic devices. Unlicensed and without independent professionals oversight, software programs are now being offered for self-analysis and treatment. Must the SBA review loan applications from firms such as these only on financial criteria? This may prove to be the effect of H.R. 1157, if passed.

203. Should the SBA be forced to approve loans to entrepreneurs of sexually explicit materials?

A recent law review commentator on the "opinion molder" rule, recommended that it be abandoned and wrote as follows:

"The SBA should consider a rule which allows all small businesses to be eligible, except those to which the grant of assistance would constitute a violation of the religious establishment clause of the first amendment.

"Under this proposal, the SBA would be forced to approve loans to qualified businesses that deal in materials which are sexually explicit but not legally obscene, such as adult theaters, bookstores and shops. Although the SBA and the majority of the American public may find it offensive and indecent, this expression is protected by the first amendment."—Julianne B. D'Angelo, "Revision of the SBA Opinion Molder Rule," 19 San Diego Law Review 801 (1982).

H.R. 1157 may accomplish precisely this law review author's recommendation. The damage that H.R. 1157 will do to the "public interest" mandate of the SBA is serious, and the safeguards H.R. 1157 appears to offer in (d)(2) may well be illusory, as will be discussed below.

The ultimate consequence of passing H.R. 1157 may well be the achievement of a situation where "the SBA would be forced to approve loans to qualified businesses that deal in materials which are sexually explicit but not legally obscene, such as adult theaters, bookstores and shops. Although the SBA and the majority of the American public may find it offensive and indecent, . . ."

Such a result is not inevitable, if H.R. 1157 is not passed. The "opinion molder" rule is a content neutral policy that suppresses no speech. The "opinion molder" rule limits federal loan subsidies to those firms satisfying agency standards of speech neutrality. This denies funds to some firms that might make good use of them, but it is not unconstitutional. There is no equal protection requirement that Congress must act mechanically to loan money to "adult" movie houses merely because Congress has elected to loan money to a bookstore.

Further, it should be noted that this law review argument, that these sexually explicit materials are constitutionally protected, is correct, but of limited relevance to the "opinion molder" rule. The cases cited by the article, *Grayned v Rockford*, 408 US 104 (1972) and *Police Dep't of Chicago v Mosley*, 408 US 92 (1972) both deal with government restrictions on speech based upon its content. The virtue of the somewhat draconian SBA "opinion molder" rule has been that it is clearly "content neutral." It excludes all "opinion molders" but for a few narrow and special cases.

For example, it exempts broadcasters and advertisers who are subjected to other government agency oversight, the FCC and FTC respectively. The other exceptions to 120.2(d)(4) are upon characteristics of the applicant that identify the applicant as "content indifferent" or "neutral," in a phrase, NOT an "opinion molder."

Thus, at the present, "opinion molders" marketing sexually explicit materials are ineligible for loans because all "opinion molders" are ineligible for loans. H.R. 1157 would eliminate this categorical exclusion from eligibility and would require an individualized determination. Even within the breadth of discretion under the spending power, an individualized disqualification of a loan applicant because the loan applicant is publishing "sexually explicit" material will invite judicial reversal. The content review of the applicant's actual speech seems to run well beyond the process qualifications approved in *Taxation With Representation*, above.

In other words, the very kind of public interest review provided by H.R. 1157 invites strict scrutiny and a finding that the agency criteria have burdened speech impermissibly and are unconstitutional.

Vagueness presents another problem for H.R. 1157. The one instance in which a federal court has found an aspect of the "opinion molder" rule unconstitutional was because of its vagueness. That deficiency has now been cured. Ironically, as we shall see next, H.R. 1157 revives the vagueness problem of the old "opinion molder" rule, and section (d)(2)(A) of H.R. 1157 is probably unconstitutionally vague.

204. Does H.R. 1157 adequately protect the "public interest?"

In (d)(2)(A) the bill permits the SBA to deny financial assistance to any applicant, if, on the basis of a hearing on the record, the SBA determines that such assistance will be "adverse or detrimental to a legitimate public interest."

What is meant by "legitimate" public interest? "Legitimate" is clearly used here as a term of emphasis, but what does it emphasize?

Does it reinforce the presumption in favor of those firms listed in (d)(1)? It would appear to have that effect.

Does it emphasize that the "opinion molder" test is NOT to be revived? As a word of contrast, it might be intended to have that effect.

Is it a cautionary term to the SBA, that the agency must not try to implement criteria that would deny loans to "adult" theaters, etc.? It may well be perceived as such.

Is it a caution against the use of "content review," emphasizing that the only "legitimate" public interests within the competency of the Small Business Administration are financial criteria? Perhaps that is its meaning, in effect to declare the intention of Congress to be to narrowly circumscribe the scope of agency review of loan applications.

The brevity and abstractness of section (d)(2)(A) will present the courts with little guidance and will make the section face a high risk of being found unconstitutionally vague by the courts.

Certainly section (d)(2)(A) has not received a very warm welcome from the friends of the bill. Mr. David Godine, speaking on behalf of the Association of American Publishers, Inc., while supporting H.R. 1157, noted in his statement for the November 15, 1983 hearings of this Committee: "We submit that there is no definition of a 'legitimate public interest' and it would be all too easy for anyone to determine for some vague reason that assistance would be 'adverse or detrimental' to this undefined public interest." Further, Steven J. Riekes, as legal counsel to the Theatre Equipment Association, Inc., also a supporter of H.R. 1157, felt it necessary in his statement for the November hearing to offer substitute language for (d)(2)(A) "to make the language more exact and to more adequately deal with any Constitutional question." What Mr. Riekes used to replace "legitimate public interest" was a limitation on gambling, illegal activities, and dissemination of obscene materials if unlawful in the relevant jurisdiction. These limited provisions hardly promise the breadth of the "public interest" implicit in the Small Business Act at this time, though it may well, as he insists, "not change the intent of H.R. 1157." It is impossible to say precisely what that intent is, the phrase "legitimate public interest" is so vague.

One thing is certain. "Legitimate public interest" does not give clear signals to the agency, to the public or to the courts. In 1976 the U.S. District Court of the Southern District of New York struck down the then applicable "opinion molder" rule. The "opinion molder" rule then read: "Financial assistance will not be granted by SBA: . . . (4) If the applicant is a newspaper, magazine, book publishing company or similar enterprise." In striking down this rule for unconstitutional vagueness, the court wrote:

"It is impossible to tell from a reading of the regulation that a bookstore would be covered by its prohibitions. In fact, under the administrative decisions and interpre-

tations of the regulation, attorneys for the SBA could not agree how the applicant was covered by the rule."

The H.R. 1157 phrase, "legitimate public interest," is just as vague as "similar enterprise." It is not enough of a standard for the agency to attempt to give meaning to it. When read against the legislative history, with the clear purpose of H.R. 1157 being to strike down the "opinion molder" rule and its attendant public interest policies, what kind of meaningful content might the agency give it?

It is my opinion that section (d)(2)(A) may turn out to be a Trojan horse.

Once judicial review of (d)(2)(A) is sought, the subsection may be struck as unconstitutionally vague. The SBA may then be confined by the courts to using only financial criteria. In such an eventuality, the ostensible purpose of (d)(2)(A), protecting the "legitimate public interests" of the public, will have collapsed, and the extent of public interest review of loan applications may be reduced to little more than accounting and financial data review.

If H.R. 1157 is passed and the SBA wishes to preserve for itself the largest range of public interest criteria, it should proceed immediately to rulemaking and establish a list of disqualifying factors by regulation, e.g., "firms promoting the sale of obscene literature." It may then try to apply these in the individual hearings on the record as to each loan application, subject to judicial review as to the implicit delegation of "legitimate public interest" and to First Amendment limitations. It could prove a litigation nightmare.

There are still other problems for the SBA. If H.R. 1157 passes, Congress will have taken away the categorical exclusions of the "opinion maker" rule. This means public interest criteria may have to be established for each particular type of firm or category of business. Not only is this very difficult to do, but it risks offending First Amendment, vagueness, rational basis and equal protection rights.

Although recent case law appears to give the government generous deference in determining what it will or will not subsidize, regulations defining limits upon the type of speech that may be subsidized will be extremely difficult to write.

Several factors complicate the process. The regulations must be narrow, lest they chill or burden protected speech. The speech interests of these firms may be commercial speech, in which case the regulations—if found to be positive controls on the First Amendment exercise—must address a substantial government interest, must directly advance this interest, and must not be more extensive than necessary to serve that interest. *Bolger v Youngs Drug Products Corp.*, 103 S.Ct. 2875, 2881 (1983). On the other hand, much of the speech of these firms will be noncommercial, even though motivated by a commercial purpose. "With respect to noncommercial speech, this Court has sustained content-based restrictions only in the most extraordinary circumstances. *Ibid.*, at 2879.

Further, the closer the SBA comes to the actual regulation of speech, the more dependent it is upon some clear indication from Congress that it was the congressional intent to give such regulatory authority to the SBA. When this inquiry arises, the courts must compare an old and very general "public interest" mandate with the language of H.R. 1157, which, if anything, raises strong presumptions against a significant delegation of speech regulating authority.

This is not to say that the material discussed in Part III of this statement, dealing with the general principles relating the First Amendment to the spending/taxing powers, is not controlling. It is merely to emphasize that this is a difficult area in which the SBA is likely to tread with great care, and treading with great care around First Amendment rights often means, prudently, doing nothing.

A very likely result, if H.R. 1157 is passed, is that the SBA will simply withdraw any significant effort to protect the "public interest" in the allocation of the federal loan monies, and will give loans to whatever firms qualify financially, whether they are "adult" bookstores, pornographic film makers, "advocacy" publishers, etc.

205. What regulatory authority is preserved by H.R. 1157's denial of loans on the basis of their being used to promote or criticize political or religious ideas?

Section (d)(2)(B) permits, though it does not require, the SBA to deny financial assistance if the SBA finds on the basis of a hearing on the record that such assistance will be "used primarily to promote or criticize political or religious ideas."

What is a promotion or criticism of a political idea?

An engineering journal regularly and extensively criticizes government procurement standards. Political? A hospital economics journal devotes most of its space to regulation topics. Political? A textbook publisher specializes in books on American history, which books are expected to maintain scholarly perspectives on society and government, and to infuse their accounts with critical judgment. Political?

Was (d)(2)(B) intended to drag back into SBA administration all of the controversies under the "opinion molder" rule? Is (d)(2)(B) designed to permit the agency to

deny loans to all but political eunuchs? Clearly not. But the legislative intent does not manifest itself in this sparse language.

If H.R. 1157 is passed, the prudent strategy for the SBA as to (d)(2)(B) would be to immediately adopt a series of regulations giving specific content to its criteria of "primarily" promoting political ideas, following the lead of the recent 9-0 Supreme Court decision in *Regan v Taxation With Representation*, 76 L Ed 2d 129 (1983).

PART III—DISCUSSION OF FIRST AMENDMENT LAW IN RELATION TO THE "OPINION MOLDER" RULE

301. Those who assert their First Amendment rights have no right to have that exercise subsidized by the government. This principle was reaffirmed by the Supreme Court 9-0 in 1983. *Regan v Taxation With Representation*, 76 L Ed 2d 129, 137 (1983).

302. The denial of a low cost loan, a tax exemption, or other subsidy for a specified exercise of a First Amendment right is not the same as a negative regulation or burdening of that right. Thus, to deny a loan to one seeking it to operate an "adult bookstore does not interfere with the applicant's right to operate an "adult" bookstore. The government may not deny a benefit to which the person is otherwise entitled because that person has exercised a constitutional right. *Perry v Sindermann*, 408 US 593 (1972). But the government may elect not to pay for the exercise of that right, as an independent policy. Thus, "Congress is not required by the First Amendment to subsidize lobbying." *Taxation With Representation*, above, at 137, citing *Cammarano v. U.S.*, 358 US 498 (1959). Applying this to the SBA, the SBA could not deny to a First Amendment enterprise a loan to which that firm was, as a matter of law, completely entitled. In such a circumstance, the SBA assertion that the applicant is an "opinion molder" would be without legal significance. It would constitute no more than an irrelevant finding of fact. But the SBA may exclude "opinion molders" from those eligible to receive loans when it has lawfully made "opinion molder" one of the disqualifying legal criteria. Even here, of course, the SBA is subject to additional First Amendment limits. The exclusion must be content neutral and must not presume to decide on the basis of the subject matter of the First Amendment exercise. *Police Dep't of Chicago v Mosley*, 408 U.S. 92 (1972).

303. When the government exercises control over its own property, provided government has not created a public forum, *Adderly v Florida*, 385 US 39 (1966); *Greer v Spock*, 424 US 828 (1976); over its taxing power, *Taxation With Representation*, above at 139; or over its power, *Taxation With Representation*, above at 139; or over its appropriations or spending powers, *Commissioner v Sullivan*, 356 US 27 (1958), the "Congressional selection of particular entities or persons for entitlement to this sort of largesse 'is obviously a matter of policy and discretion not open to judicial review,' absent special circumstances. *Taxation With Representation*, above at 139. Thus, it is not for the courts to displace the discretion of the SBA in determining the public interest as to loans, even when SBA policy deliberately excludes (uniformly and without content review) First Amendment enterprises from loan eligibility, so long as the SBA exercise is properly within its rulemaking delegation from Congress.

304. Equal protection principles do not require that when government subsidizes one category of firms that it must subsidize others, even though the excluded firm is engaged in the sensitive exercise of First Amendment rights. As a matter of policy, Congress may decide to give an organization "dedicated to combating teenage drug abuse" a money grant, conditioned upon the requirement that none of the money received may be used to lobby a state legislature. Congress may then provide "public money for an organization dedicated to combating teenage alcohol abuse," and impose no condition against using funds obtained from Congress for lobbying. The different statutes are products of legislative policy and neither violate equal protection nor do they require strict scrutiny. *Taxation With Representation*, above at p. 138. Thus, that the SBA loans money to general bookstores does not require them to loan money to newspapers.

305. The proper standard for judicial review of statutory classifications that neither interfere with a fundamental right nor employ a suspect classification is merely rational basis. *Taxation With Representation* above at 137-138.

306. An agency regulation very similar to that of 120.2(d)(4) of the SBA is Section 501(c)(3) of the Internal Revenue Service. Both regulations impose standards of content neutrality upon the recipient of benefits, although the IRS regulation grants the tax exemption to a broad array of organizations that would be termed "opinion molders" by the SBA. Since a neutrality standard has been employed in connection with each, and since each has been subjected to First Amendment attack, the think-

ing of the courts in applying 501(c)(3) is relevant to understanding 120.2(d)(4). The 501(c)(3) cases tend to confirm the discretionary powers argued on behalf of the SBA in this statement to the Subcommittee. In addition to *Regan v Taxation With Representation*, 76 L Ed 2d 129 (1983), relied upon extensively above, three illustrative cases of additional aspects 501(c)(3) litigation may be instructive. *Haswell v United States*, 500 F.2d 1133 (1974) (holding tax exemptions to be matters of grace, that taxpayer's activities were not "nonpartisan analysis, study, or research," and hence did not qualify for the exemption under the regulations). *Big Mama Rag, Inc. v United States*, 631 F.2d 1030 (1980) (holding that an IRS neutrality requirement of "full and fair exposition" was unconstitutionally vague). *National Alliance v United States*, 710 F.2d 868 (1983) (holding that an organization dedicated to "arousing in white Americans of European ancestry 'an understanding of and a pride in their racial and cultural heritage'" did not qualify as a charitable or educational organization under IRS regulations controlling tax exemption eligibility). These cases tend to show that a much more subtle and positive review of tax exemption seeking First Amendment protected organizations has been undertaken by IRS than in the rather simple and broad categories used by the SBA, and yet the IRS regulatory scheme has been found constitutional and the neutrality requirements have been generally upheld by the courts. This suggests that the "opinion molder" rule is substantially less threatening to First Amendment values and rights than is frequently suggested by those who dislike that rule.

APPENDIX TO:
STATEMENT OF ROBERT E. PARK
BEFORE THE SUBCOMMITTEE ON
EXPORT OPPORTUNITY AND SPECIAL
SMALL BUSINESS PROBLEMS
OF THE
UNITED STATES HOUSE OF REPRESENTATIVES

May 31, 1984

- PART IV -

FURTHER COMMENT AS REQUESTED

In the course of my appearance before the Committee, Congressman Vandergrieff expressed an interest in having my comments on S. 2084, the Senate bill introduced to change the "opinion molder" rule of the Small Business Administration. I am pleased to provide those comments in this appendix.

I have prepared my comments upon S. 2084 following the format of my comments on H.R. 1157. Since the two bills have some of the same consequences, I have referred to the appropriate sections in my original statement to avoid repetition of those comments. Sections 402, 403 and 404, in particular, refer back to earlier comments.

In introducing these comments I might note that the Department of Justice provided Senator Lowell Weicker, Jr., at his request, with its views of S. 2084. I was asked by the Staff of the Senate Committee on Small Business to respond to the views of the Department of Justice. I have included my response to those views in this supplemental material as section 406.

SUMMARY OF MY COMMENTS ON S. 2084 -

S. 2084 would compel the SBA to abandon its "opinion molder" rule and would substitute a series of three tests to protect the public interest, at least one of which tests would invite litigation and would be difficult for the agency to administer without violating First Amendment protections. S. 2084 explicitly bars the SBA from denying financial assistance to certain categories of small business for the reason that the firms are engaged in those businesses, e.g., book publishers, record production, motion picture theaters, etc. S. 2084 has been supported, among other reasons, because the present SBA regulations sweep so broadly as to exclude from loan eligibility many innocuous businesses, e.g., neighborhood movie theaters. While reversing existing SBA policy, this statutory provision is clearly within the power of Congress. S. 2084 then provides three grounds upon which SBA might deny financial assistance to any small business concern. These grounds are within the constitutional powers of Congress, but present three important and controversial policy problems. First, S. 2084 will require SBA to make government loans to

"adult bookstores," producers of sexually oriented films, publishers advocating pederasty, sado-masochistic sex, eugenic legislation, infanticide, etc., and other highly controversial enterprises that present SBA policy insulates from federal loan subsidies. If it is not the intent of Congress to associate itself and the federal government with the financial support of businesses dedicated to or serving primarily such markets, then Congress may wish to consider carefully whether or not S. 2084 will compel this result. It is my strong impression that this will be the unavoidable effect of S. 2084, as it is now worded. Second, S. 2084, while appearing to permit the SBA to avoid the subsidization of illegal activities and the dissemination of obscene materials, S. 2084 actually imposes a heavy burden upon the SBA to make extremely difficult constitutional findings and conclusions. These issues may be fairly characterized as "litigation inviting" findings. It is a job for which the SBA is ill suited and which is quite foreign to its central mandate, which is the support of the development of small businesses. Further, since the findings necessary to avoid extending financial assistance to illegal gambling enterprises and publishers of obscene materials essentially depend upon predictions by the SBA as to what a jury will do in a criminal trial with its "beyond a reasonable doubt" standard of proof, it may prove difficult for the SBA to develop an adequate record in its informal administrative proceedings that will satisfy due process, as applied in the course of judicial review. Judicial review, of course, is a feature of S. 2084. Further, since the grounds upon which financial assistance is to be denied require an individualized review of the applicants conduct, rather than a categorical exclusion by rule, it draws the agency perilously close to content review of the particular opinions or activities of the loan applicant. This aspect of the administrative process is quite distinct from the abstract constitutional power of the Congress in the exercise of its taxing and spending powers to give or withhold benefits to categories of its choice. Thus, the abstract constitutionality of the statute will not protect the agency from intense litigation over particularized agency findings as to the categories provided in S. 2084 for denying financial assistance. The First Amendment risks are heightened in applications of tests of illegality or obscenity. Content neutral rules are easier to administer without offending the Constitution. The "opinion molders" rule and the exclusion of "advocacy" bookstores are examples of content neutral rules. Further, any rules adopted pursuant to the administration of S. 2084 are certain to be highly controversial and are likely to be challenged. Constitutional questions of equal protection, vagueness, overbreadth and underinclusiveness, the free speech clause, and of the freedom of the press will be tested against any SBA asserted public interest. Under S. 2084, either the SBA will have to abandon or dilute its conception of the public interest. Put plainly, the practical effect of S. 2084 may well be to deny the SBA the power to adopt any public interest regulation controlling loan policy unless a) the applicant has breached the narrow grounds of S. 2084 (essentially, the applicant must be engaged in illegal conduct or extending the loan must be unconstitutional as offensive to the establishment clause) or b) the disqualifying factor is purely an objective, accounting type limitation. Worse, even if only regulations as to illegal or obscene materials are adopted, it is my belief that, in spite of the bill's facial constitutionality, the SBA will become involved in difficult

constitutional litigation testing the agency findings of the illegality of the applicant's conduct or of the obscene nature of its products, diverting the SBA from its principal responsibilities, which are the business and financial assistance of small businesses. A third concern that S. 2084 may raise in some observers is that, for the businesses named in the bill, as worded, it may appear that Congress intends that these businesses shall be subject to no other constraints on financial assistance than those explicitly identified in S. 2084. I think such a reading inconsistent with the announced intent of the bill's sponsors, but a plausible and perhaps necessary reading of the plain language of the bill. This result of S. 2084 would take the "skin flick" movie operator from an excluded business under SBA loan policy to a preferred position. It is hard to believe that this would be the intent of Congress, but the possibility suggests the need for additional language in the bill.

DISCUSSION OF THE PROVISIONS OF S. 2084 -

401. Although constitutional as a statute, S. 2084 would present the SBA with extremely difficult and litigation provoking problems of administration, which administrative problems inescapably would raise constitutional issues in themselves.

As discussed in Part III of this statement, the Congress enjoys broad constitutional discretion in its decisions to afford tax or grant benefits. Congress may condition subsidies, such as those underlying the SBA loan program, in practically any rational manner that it chooses, so long as it does not use such programs to contrive a negative impingement upon someone's constitutional rights. The restrictions in S. 2084 have no such negative consequences, so the statute is constitutional on its face.

S. 2084 provides three tests that may be used to deny financial assistance to the small business concerns named by type in the bill. Each test will be discussed briefly, but the problems raised under Test A and Test B also apply to Test C, and the difficulties of all three tests should be reviewed together.

Test A permits, but does not require, the SBA to deny financial assistance to businesses when "such assistance will be used primarily to advance or inhibit religion." This determination is individualized to the applicant for the loan, and can be made only after a hearing.

First, is the advancement or inhibition a question of fact, of law or a mixed question of law and fact? Clearly a mixed question. The SBA is not the final decision maker on conclusions of law. This test permits judicial second guessing of agency decisions, and therefore invites litigation. Examples may be helpful. Assuming that these newspapers were small enough businesses to qualify, would THE CHRISTIAN SCIENCE MONITOR be excluded from loan eligibility under this test? THE WASHINGTON TIMES? A newspaper devoted to reporting church affairs and to printing devotional articles, but which was clearly a commercial enterprise? A publisher of bibles and religious books that is clearly a profit oriented business? This problem is of limited interest because

it is not likely to occur often, but the uncertainties demonstrate why a clear and constitutionally satisfactory test, such as Test A, may be controversial in application and might become an administrative horror.

Second, is "primarily" an objective statutory test, or is it a judgment call? Does it imply discretion? If it implies discretion, does it raise risks of discrimination or arbitrariness in the sensitive area of religious organizations? If it is not a judgment call but presumes to be an objective test, does it invite judicial second guessing as to the definition of what will satisfy the "primarily" test?

The "primarily" test as to the use of financial assistance parallels the establishment clause cases, and the parallel as to Test A (enhancement or inhibition of religion) is clear. *WALZ v. TAX COMM'N*, 397 U.S. 664 (1970); *COMMITTEE FOR PUBLIC EDUCATION & RELIGIOUS LIBERTY v. REGAN*, 444 U.S. 646 (1980). It is not, however, a very satisfactory parallel as to Tests B and C of S. 2084. In the establishment clause cases, "primary effect" is used as a negative complement to the test of "secular purpose." But the residual or incidental effects in those cases have been socially benign. In Tests B and C, by way of contrast, the conduct in question is illegal and socially malignant. It is presumably not the intent of the sponsors of S. 2084 that the SBA is only to deny loans to subversive organizations when the "primary effect" of the loan itself is to promote the subversion of government. Similarly, it is presumably not the intent of the sponsors of S. 2084 that the SBA is only to deny loans to disseminators of obscene materials when the "primary effect" of the loan itself is to immediately and directly to facilitate the distribution of obscene publications.

Test B permits, but does not require, the SBA to deny financial assistance to business concerns when such assistance will be used primarily to threaten the overthrow of organized government by unlawful means. This determination, too, is to be made on an individualized basis, after a hearing.

What kind of record is necessary to establish that a particular concern will use its financial assistance primarily to threaten the overthrow of the government by unlawful means? What standard of proof will control? Preponderance of the evidence, as is normal in administrative proceedings? Clear and convincing evidence, as is now required in some areas of sensitive individual rights? While due process is not likely to require that the proof of unlawful means meet the criminal standard of beyond a reasonable doubt, the sensitivity of the issues may encourage an extraordinarily intensive and thoroughgoing judicial review, even if the nominal test remains the normal preponderance of evidence standard.

As to another aspect, the effective investigation and presentation of evidence relative to rejecting applications would require proving illegal conduct, and the statutory basis for such illegal conduct could vary radically from one case to another and cover the whole range from federal law to the state law of 50 jurisdictions. This unfamiliar and time intensive responsibility would be severely burdensome to the SBA. Indeed, with its limited coercive powers, one might reasonably ask

whether the SBA can build an adequate record as to proving criminal misconduct. If this enforcement burden proves too heavy, the SBA may be inclined merely to standby and await a judicial determination. This caution would frustrate the statutory policy, of course, but might well emerge as the SBA practice in this controversial area.

Since extremely sensitive First Amendment rights of speech and of association may be threatened by this administrative proceeding, the courts are not likely to see very much administrative expertise in this area to which they should defer. Indeed, the loyalty oath cases and Communist conspiracy trials show that this apparently clear statutory standard could become treacherously complicated in application. Is this the kind of inquiry that Congress wishes to impose upon the SBA small business loan program?

The standard of proof problem especially haunts Tests B and C, for both involve "illegality" tests as requirements for SBA denials of assistance.

Test C permits, but does not require, the SBA to deny financial assistance to any small business where (1) such assistance will be used primarily (2) to engage in any illegal activity or (3) the dissemination of obscene materials (4) which may be unlawful in any jurisdiction in which the small business concern (5) may operate. Here, as in the other two tests, an individualized determination, based upon a hearing, is required.

We note that in Test C both elements (2) and (4) raise questions of illegality. These problems were discussed under Test B, but also apply here and with special force.

It is worth noting before discussing Test C that S. 2084 is not the only constitutional way to disqualify businesses disseminating obscene publications. Three other options should be noted. Each is more flexible than S. 2084, and more amenable to protecting broader and unexpected but important aspects of the public interest. 1st, a broad exclusion of "opinion molders," as the SBA has done, is constitutional. See Part I, above. 2nd, a more narrow exclusion of "promoters" or "advocates" of ideas, would also appear to be constitutional. See section 105, above. 3rd, relying upon the broad constitutional discretion of Congress to tax or grant benefits, an exclusion framed in terms of "sexually oriented" materials might also satisfy the First Amendment. See Part III, below. In any case, the point is important that S. 2084 not be perceived as the only constitutional option in dealing with firms seeking government loans. None of these three options just discussed imposes upon the SBA the difficult burden of proving illegal conduct, a burden that will be central to denying loan applications to these preferred businesses under S. 2084.

We must discuss further the especially difficult issues the SBA will meet in having to prove that material is obscene. Historically, appellate courts have been quick to review trial courts' findings of "facts" as to obscenity. They will be even more sensitive and quick to review an administrative agency's findings of obscenity. And rightly so.

Further, under *MILLER V. CALIFORNIA*, 413 U.S.15 (1973), the U.S. Supreme Court abandoned any expectation that standards as to what appeals to the prurient interests or is patently offensive can be "articulated for all 50 states in a single formulation." This means that the SBA must master the local obscenity standards for every jurisdiction in which the applicant firm does business or to which it sends its publications or films. As to firms doing business in numerous states, must the SBA bring to Washington, D.C., or to the state in which the hearing is held, witnesses from distant states to prove that the applicant has engaged in the unlawful dissemination of obscene material, or has otherwise acted unlawfully?

Does the SBA have the resources to protect even S. 2084's narrow conception of the public interest under the unlawful obscenity test of S. 2084? Clearly not. The consequence of S. 2084 will be, in all probability, the abandonment of public interest standards. The SBA will be driven by necessity to merely accounting and financial standards.

402. S. 2084 would require the SBA to make loans now denied and would exclude from application to the named types of businesses the public interest standards now available under the Small Business Act.

Similar objections may be raised to S. 2084 as were raised to H.R. 1157 in section 201 of my statement, above. It is clear that S. 2084 may have the effect of changing the implications of the congressional "public interest" mandate to the SBA.

403. How S. 2084 might change the way SBA considers loans.

Similar objections may be raised to S. 2084 as were raised to H.R. 1157 in section 201 of my statement, above.

404. Should the SBA be forced to approve loans to entrepreneurs of sexually explicit materials?

Similar objections may be raised to S. 2084 as were raised to H.R. 1157 in section 203 of my statement, above.

405. Test C of S. 2084 permits the SBA to deny a loan only when the financial assistance will be used "primarily" to engage in any illegal activity, e.g., gambling, or the dissemination of obscene materials, raising an uncertainty as to the meaning of primarily.

May a firm engaged in illegal gambling obtain an SBA loan for the legal aspects of its business? May a firm that disseminates obscene materials use the SBA loan to buy its building, rather than for printing presses? May an illegal gambling establishment borrow funds from the SBA for the limited and explicit purpose of redecorating its restaurant? May a whorehouse get an SBA loan to buy vans? An espresso coffee machine?

Is the test "primarily" introduced to avoid problems of indirection and causality? Does it introduce inescapably complex issues

as to the degree or extent of the firm's involvement in the forbidden activity? It would appear to have been introduced as a scrupulous test, avoiding trivial or borderline cases, but its effect may be to introduce more problems than it resolves. Is a bookstore that only obtains 5% of its net profits from unlawful obscene materials eligible for a loan? 20%? Is a nightclub that only occasionally permits illegal gambling on the premises eligible?

Similar questions may be raised as to Tests A and B.

406. The Department Of Justice Advisory Letter on S. 2084.

Members of the Committee Staff of the Senate Small Business Committee asked that I respond to a letter of 12 March 1984 to Senator Lowell Weicker, Jr., Committee Chairman, from Robert A. McConnell, Assistant Attorney General, Office of Legislative Affairs. Mr. McConnell's letter was in response to an inquiry by Chairman Weicker seeking the Department of Justice's views on S. 2084. As previously noted, this bill has been offered "to restrict the authority of the Small Business Administration" (SBA) as to its discretion in denying financial assistance to small business concerns. My compliance with the staff request is provided here as complementary to my comments upon S. 2084 for the House of Representatives Subcommittee on Export Opportunity and Special Small Business Problems.

The Department of Justice Opinion -

The advisory opinion from the Department of Justice gave two reasons why this bill should not be enacted:

First, the standards for denying financial assistance under the bill are very broad and vague, and as such, may prove difficult to administer, as well as occasion many judicial challenges to the Administration's determinations of financial assistance. Secondly, as a constitutional matter, these standards appear to be impermissibly vague and fail to comport with the strict standards required when limits are placed on the First Amendment activities of individuals, including recipients of governmental funds. Although the applicable standard of scrutiny in such cases remains unsettled by the courts, it is likely that under even minimal scrutiny the standards outlined in this bill would fail constitutional muster.

The Department implied an important distinction in separating these two reasons. The question of whether or not a statute will be difficult to administer is quite distinct from whether or not the statute is constitutional. Further, the administration of a statute may itself raise constitutional issues, even though the statute creating the regulatory scheme is fully constitutional.

In my comments upon the advisory opinion from the Department of Justice, I will agree with the Department as to their first reason for

opposing enactment of S. 2084, that the bill will be difficult to administer. I will disagree with the Department as to their second reason, for, unlike the Department, I do not believe that this bill is unconstitutionally vague.

The First Reason: Difficulties in Administration -

This discussion will be more intelligible if we note explicitly some of the language of S. 2084:

The Administration may deny financial assistance to any small business concern . . . if the Administration determines, after an opportunity for hearing, that such assistance will be -

- (A) used primarily to advance or inhibit religion;
- (B) used primarily to threaten the overthrow of organized government by unlawful means; or
- (C) used primarily to engage in any illegal activity or the dissemination of obscene materials which may be unlawful in any jurisdiction in which the small business concern may operate.

Three types of situations may arise in the SBA's administration of S. 2084. First, where a court of law has made the critical finding of fact of illegal conduct necessary to invoke the criteria of the S. 2084, the SBA may rely upon such findings. Second, where the agency suspects that the applicant is guilty of the kind of illegal conduct described in S. 2084, but no court has made such a finding, then the SBA must make such a determination of fact (really a mixed question of law and fact) in its own administrative proceedings. Third, where the applicant has affiliations with religious or anti-religious organizations or has engaged in religious activities sufficiently to support a finding of fact that the funds will be used primarily to advance or inhibit religion, the SBA may make such a determination of fact in its own administrative proceedings.

In the first type of situation, where the applicant has already been found to have engaged in unlawful conduct by a court of law, the agency's decision may be made confidently and with minimal risk of being overturned upon judicial review. The administrative difficulties in such a situation would be minimal.

In the second type of situation, where the agency must build a record of its own sufficient to support the critical finding of fact (or mixed question of law and fact) of illegal conduct on the part of the applicant, the SBA must prove unlawful conduct under the standards of federal law or of the law of the local jurisdiction. This burden would be a heavy one. The field officers, charged with making recommendations on these applications, and the hearing officers or Administrative Law Judges presiding over the hearings, would find this a difficult administrative problem. Further, since the finding of unlawful conduct would be both beyond the expertise of the agency and within the normal competency of the courts, one could expect judicial review to be both intense and largely lacking in the normal deference

afforded administrative agency decisions. These agency decisions would invite litigation.

These risks of litigation and of intense constitutional review of the SBA's administration of S. 2084 might produce a further complication. To minimize litigation and the risk of judicial reversal, the SBA might refuse to attempt to enforce even the very modest public interest standards of S. 2084, except in situations of the most blatant and embarrassing violations of the S. 2084 standards.

One might reasonably ask whether or not the SBA might not overcome the difficulties of administration by adopting carefully drafted regulations to objectify the treatment of applications? To some degree this is possible. A more fundamental problem persists, however, in that the central difficulty as to administration arises from the burden upon the agency of making findings relative to violations of laws, often criminal laws and, worse, criminal laws defining the highly controversial boundary between constitutionally protected speech and association and constitutionally unprotected conduct, when these laws are well beyond the normal competencies of the agency and beyond its expertise.

Further, as we noted above, attempts by agencies to objectify and rationalize a regulatory scheme, particularly in the sensitive area of First Amendment concerns, may create a variety of new problems, including new constitutional difficulties. This is what happened, for example, when the Department of the Treasury adopted regulations pursuant to its administration of Section 501(c) of the Internal Revenue Code. See *BIG MAMA RAG, INC. v. U.S.*, 631 F.2d 1030 (1980), one of the cases relied upon by the Department of Justice in its advisory comments concerning S. 2084.

In the third situation, where the agency finds the applicant likely to use the funds to "advance or inhibit" religion, the courts' characteristic high sensitivity to any risk of an "establishment" of religion by government is likely to afford the SBA a broad discretion in its findings of fact on this issue.

As I had noted in my written statement and oral testimony to the Senate Committee on Small Business prior to seeing the Department of Justice letter, I agree with the Department of Justice that S. 2084 would present serious administrative problems. I believe that the administrative problems are likely to prove especially difficult as to tests (B) and (C). I would note, again, that test (C) would require the SBA to master a broad range of law not germane to its primary mission of affording assistance to small businesses, and that this broad range would include both federal law and the law of each of the 50 states. Further, even though the statute provides only that the SBA "may deny financial assistance" under the tests (A)-(C), there is an implication that the SBA would be expected to apply these criteria in the public interest. That is a staggering responsibility to impose on the SBA.

The Second Reason: The Possible Unconstitutionality of S. 2084 -

The second reason given by the Department of Justice turns upon the Department's perception of S. 2084 as impermissibly vague and lacking adequate protection of First Amendment activities.

As part of the legislative history, it is worth noting that S. 2084 is not an attempt to delegate broad regulatory discretion to the SBA. Indeed, the bill has been proposed explicitly to confine the present discretion of the agency. The criteria of S. 2084 for denying financial assistance are much more narrow than those under the existing legislation, which is presumptively constitutional.

The criteria of S. 2084 for the denial of assistance turn upon findings that the assistance will be used primarily to accomplish illegal conduct as defined by state or federal law or upon a finding that the assistance will be used primarily to advance or inhibit religion. It is difficult to see how these are unconstitutionally vague.

In this discussion of the constitutionality of S. 2084, it is worth noting that S. 2084 does not attempt to delegate to the SBA the power to enact criminal legislation. Indeed, it is beyond the constitutional power of Congress to make such a delegation. The unlawful conduct of tests (B) and (C) of S. 2084, which, with (A), are the limited bases upon which the agency may deny financial assistance to small businesses, are to be defined by independent state and federal statutes, not by SBA regulations. That these statutes may be unconstitutional affects the administration of S. 2084, but does not make S. 2084, itself, unconstitutional.

The Department cited two cases in support of its conclusion that S. 2084 "would fail constitutional muster."

In *HYNES v. MAYOR OF ORADELL*, 425 U.S. 610 (1976), the U.S. Supreme Court struck down an ordinance requiring "recognized" charitable or political canvassers to afford the city advance notification before making such a canvas. The ordinance was held void on vagueness grounds, but the Court noted that the government interest in such regulation was substantial and suggested that such an ordinance, had it been drawn with "narrow specificity," would have survived the constitutional attack.

Thus, the key to the constitutional attacks over the criteria of S. 2084 must focus upon the laws defining the illegal conduct upon which the SBA must rely in denying the financial assistance. It would appear that S. 2084, itself, is quite conservatively drafted. S. 2084 conditions the denial of financial assistance upon statutes which, as relied upon, must pass high standards of constitutional review.

In *BIG MAMA RAG, INC. v. U.S.*, 631 F.2d 1030 (D.C. Cir. 1980), a U.S. Court of Appeals reviewed treasury regulations that attempted to implement a statute permitting tax exemptions to certain religious,

charitable, scientific, etc., organizations. 26 U.S.C. Section 501(c)(1976). The court concluded that the regulations were excessively vague in that they relied upon indefinite and highly subjective criteria, such as whether the organization provided "instruction of the public on subjects useful to the individual and beneficial to the community," and, when such organizations were dealing with controversial subjects, whether the organization afforded a "full and fair exposition" of the subject matter. Treas. Reg. Sections 1.501(c)(3)-1(b) & (c) (1959). S.2084 does not require any such subjective or content oriented review. In this sense, the BIG MAMA case would appear to be of limited value in assessing the constitutionality of S. 2084.

It should be noted that the above discussion does not suggest that constitutional problems may not surround the administration of S. 2084, nor that its administration may not invite litigation. But these problems arise out of the prospective administration of the bill and point to no intrinsic constitutional defect of S. 2084.

Summary of Comments Upon The Department of Justice View of S. 2084 -

Briefly, I agree with the Department of Justice that S. 2084 would present very substantial problems in its administration. I cannot agree with the Department's second reason for opposing S. 2084, since I do not find the language of S. 2084 unconstitutionally vague. S. 2084 would appear to me to afford as much notice of forbidden conduct as the statutes upon which it must rely. Further, it affords the Administrator no more discretion in targeting those to be disqualified than do than those same statutes that establish the illegality of the conduct of the applicant. Finally, as the Department concedes, the applicable standards of scrutiny of such regulatory schemes are still undetermined by the courts. My reading of *REGAN v. TAXATION WITH REPRESENTATION*, 76 L ED 2d 129 (1983), discussed in my earlier statement, suggests that the U.S. Supreme Court would permit the SBA a reasonable latitude in administering this statutorily directed program of government largesse, and that S. 2084 would be found constitutional.

The End of the Appendix

Mr. IRELAND. Well, Professor, I think you have helped us gain an insight into the whole affair. As we move along here, let me ask Mr. Vandergriff if he has any questions.

Mr. VANDERGRUFF. Well, I've been most interested in your comments, Professor Park, and thank you so much. In your testimony it seemed to me you were having some trouble, yourself, in the area of bookstores.

Mr. PARK. Yes.

Mr. VANDERGRUFF. I guess even professors' opinions when you write books tend to advocate.

Mr. PARK. I think books are naturally going to be advocating positions, and that is why I think the publishers are not included in the present SBA exemption. The bookstore sees itself as a retailer. They stock whatever people want to buy, at least the "general" bookstore does, and since they display lots of books they do not see themselves as "opinion molders." I personally don't find that very persuasive criteria. It is, however, one that the SBA uses. My feeling is simply that it's a question of purpose—why they're in business. Since these bookstores display or offer book inventories indifferently, they are content indifferent. It seems to me that it's proper for the Government to loan them money. But if you picked up a theme in the inventory, if it is a feminist bookstore, an environmental bookstore, a Republican bookstore, or a Democrat bookstore. You made him go away.

[Laughter.]

Mr. PARK. It seems to me that the SBA has concluded that then you have a ground for disallowing the application for the loan. But that was the approach I was trying to criticize. I don't think that you can constitutionally do it on the nature of the books. I think that that not only is impossible to make sense of, but that it is probably unconstitutional. I think what you have to focus on is the enterprise, and that is why I suggested this notion of "promotion" or "advocacy" as the test. The advocate, the fanatical bookstore, the fanatical movie house, the skinflick movie house, in each of these as a matter of fact you can detect a theme of "promotion" or "advocacy", and that is your best disqualifier. The occasional X-rated film in a little theater in Texas, it seems to me, should not be disqualifying. But if they do it too often, they become "promoters" or "advocates," or "opinion molders" in the language of the SBA. It seems to me that Congress and the public would not want Government money in such businesses.

Mr. VANDERGRUFF. And yet you talk about categorizing, and to carry that just a step beyond, all those theaters would be banned. You spoke in behalf of categorization if I recall.

Mr. PARK. Oh, yes, because the Constitution requires, as I understand it, a content neutral rule. The category must not refer to the content of the material, and for that reason I find the SBA's proposal that 30 percent of revenue from pornographic movies disturbing because, although it is an objective measurement, in a sense, and therefore, content neutral at that level, the way you must determine whether they met the 30 percent is to make an evaluation of the movie, that it was pornographic. Can you imagine an auditor from the SBA trying to decide whether a film is pornographic?

Mr. IRELAND. There's a gentleman right there that wants the assignment. [Laughter.]

Mr. PARK. So I find that the determination of what is obscene is a practical problem of administration, and one that you just shouldn't drop on the SBA. I don't think they can handle it.

What I was trying to suggest to the committee was that you need what I call a process rule, and that is the notion of a test of "promotion" or "advocacy" of ideas. This test can be applied without reference to content, whether it's good or bad. We are just not going to give Government money to thematic bookstores, to thematic movie houses, to thematic greeting card publishers and so forth.

That the greeting card publishers are a problem, on first blush, startles one. I mean, reading these OD's from the Small Business Administration you say, "greeting cards?" But you understand, as soon as you probe the ground rules, what it is that concerns them. They're afraid of walking into a situation where they can't make a discrimination. Line drawing in this area is just treacherous.

Mr. VANDERGRIFF. Well, now, I am having trouble in making sure that I understand correctly.

Mr. PARK. Yes.

Mr. VANDERGRIFF. It's my fault, I am certain.

Mr. PARK. No.

Mr. VANDERGRIFF. But I hear you saying that there are two different types of theater houses, for example, and that there ought to be a way to assist a certain type.

Mr. PARK. I tried to suggest a way to assist one type, but not the other, and that is to ask, "Does this theater management program films that show a continuing theme." If it does it would be disqualified just as the bookstores that "promote and advocate" are disqualified.

Mr. VANDERGRIFF. Well, I really think perhaps together with your assistance and the committee's efforts, we can provide a basis on which the SBA can differentiate.

Mr. PARK. Congressman, I think if they took their book rule, and they applied it to movie houses, the present rule would do the job. But not in the sense of specialization, for the "specialist bookstore" is not an informative category. I don't know what a specialist bookstore is. That is why I tried to deal with it in the statement. A medical bookstore is a specialist bookstore, and I think a medical bookstore should get a loan. A medical bookstore that carries controversial books about abortion or AIDS or abused children, it seems to me should get a loan. But once the medical bookstore establishes itself in terms of a cause, adopts a theme, has a mission, plays to a particular "opinion" constituency, at that point it seems to me it should be disqualified.

Mr. VANDERGRIFF. But if it has a few of those controversial medical theories—

Mr. PARK. No problem.

Mr. VANDERGRIFF. You have no problem with it.

Mr. PARK. No problem. Indeed, the general bookstore is full of philosophy, isn't it?

Mr. VANDERGRIFF. Oh, yes, certainly.

Mr. PARK. So it is not the books that are the problem. It's the purpose of management that it seems to me is the problem.

Mr. VANDERGRIF. All right. One last question. We asked it of the SBA itself, and I believe Mr. Sanders' statement was he was going to be briefed on it on Friday. Had you seen S. 2084?

Mr. PARK. Congressman, I am sorry. I went through what I was provided, your staff had kindly mentioned that the Senate has legislation pending, but I have not seen that.

Mr. VANDERGRIF. You have not seen that proposal?

Mr. PARK. I have not seen that proposal.

Mr. VANDERGRIF. I would be very pleased to look at it and make a supplemental comment.

Mr. PARK. Thank you, sir. Thank you, Mr. Chairman.

Mr. IRELAND. Indeed, with your permission, Professor, we might suggest to them that they give you a telephone call if not send a car for you. [Laughter.]

Mr. IRELAND. Let me ask you another question following up on the theme idea and the purpose of management. At our previous hearing on this subject, we had a witness, Mr. Scott, of Scott's Law Books, Inc.

Mr. PARK. Yes.

Mr. IRELAND. Is that a theme?

Mr. PARK. No. I found that a disturbing piece of testimony. I felt that the law book firm is very much in the situation of the medical book firm. It seems to me that they will have thematic material in their inventory. It will be controversial and take viewpoints, but as long as the bookstore doesn't take a viewpoint they should be eligible for loans. Suppose I organize the bookstore to promote civil rights, and I had all the titles that were in print on civil rights. I should not get an SBA loan because it is a thematic bookstore. It is, in the language of the SBA regulation, it seems to me, promoting and advocating. If I have a legal bookstore, and it has everything, politically right to left, you know, crazy to dull, I should be able to get an SBA loan.

Mr. IRELAND. In your view then, most of this could be handled by the SBA rethinking, fine-tuning maybe is the word, its regulation or substantial part. I mean this isn't a 100-percent thing, but they went through with this purpose of management theme idea, and they could clear away a lot of cobwebs.

Mr. PARK. Congressman, I think so. I had tried to suggest in my statement that I saw essentially three options for Congress. One is to essentially continue to monitor the SBA and put pressure on them, to make some accommodation, to adapt its procedures to enlarge the class of eligibles, for these are legitimate and fair demands on the part of the public to participate. I think that is the safest course. I think a bill that would substantially reshape the meaning of public interest, such as H.R. 1157, will frighten the SBA out of public interest administration. My concern is that H.R. 1157 will make it too attractive for the SBA to abandon public interest analysis and to administer the program on purely financial criteria. I am sure that the SBA would be relieved if they didn't have to worry about whether it was an adult bookstore or not, and could just look at the account books, so to speak. Now it seems to me that one of the dangers of H.R. 1157 is that it will gut the public inter-

est. At the least it would take enough of the content out so as to make the SBA anxious and defensive about applying "public interest" tests in the loan process. And this would be particularly the case if you couple weakening the public interest test with the addition of hearings on the record, to be heard by administrative law judges, and all the other costs and delays. So, were I given the choice, I would press the SBA to try to accommodate what reasonable people see as a fair——

Mr. IRELAND. Thank you, Professor. We certainly appreciate it. At this point if there is no objection by Mr. Vandergriff I'd like the gentleman from the SBA to carry the word back, and if he will put it in written form, for the SBA to respond to this thought of changing the regulation within the thematic purpose of management approach and the SBA's on-hand comment.

Mr. HERTZBERG. We'd be very pleased to look very carefully at that and give it full consideration. I found the professor's testimony very interesting.

Mr. IRELAND. Fine. Thank you so much.

Mr. PARK. Thank you.

Mr. IRELAND. I would like, before we conclude, without objection to put in a very brief statement from the Alabama Independent Business Association for the record. Mr. Vandergriff, anything further?

Mr. VANDERGRIFF. No; nothing further.

Mr. IRELAND. We are adjourned. Thank you.

[Whereupon, at 11:25 a.m., the subcommittee adjourned, to reconvene subject to call of the Chair.]

APPENDIX

I

APPENDIX A

98TH CONGRESS
1ST SESSION

H. R. 1157

To amend the Small Business Act to restrict the authority of the Small Business Administration to deny financial assistance to small business concerns solely because the primary business operations of such concerns relate to the communication of ideas.

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 2, 1983

Mr. ADDABBO introduced the following bill; which was referred to the Committee on Small Business

A BILL

To amend the Small Business Act to restrict the authority of the Small Business Administration to deny financial assistance to small business concerns solely because the primary business operations of such concerns relate to the communication of ideas.

- 1 *Be it enacted by the Senate and House of Representa-*
- 2 *tives of the United States of America in Congress assembled,*
- 3 That section 4(d) of the Small Business Act (15 U.S.C.
- 4 633(d)) is amended to read as follows:
- 5 “(d)(1) Except as provided in paragraph (2), the Admin-
- 6 istration may not deny financial assistance under this Act to
- 7 any small business concern solely because the primary busi-

1 ness operation of such concern is book, newspaper, magazine,
2 greeting card, or history calendar publication or distribution;
3 radio or television broadcasting; film, record, or video tape
4 production or distribution; instruction or tutoring academic
5 subjects; or any other similar operation.

6 “(2) The Administration may deny financial assistance
7 to any small business concern referred to in paragraph (1) if
8 the Administration determines, on the basis of a hearing on
9 the record, that such assistance will be—

10 “(A) adverse or detrimental to a legitimate public
11 interest, or

12 “(B) used primarily to promote or criticize politi-
13 cal or religious ideas.

14 “(3) Any small business concern which is denied finan-
15 cial assistance pursuant to paragraph (2) of this subsection
16 shall be entitled to judicial review in accordance with chapter
17 7 of title 5, United States Code.”.

APPENDIX B.—PREPARED STATEMENT OF STEVEN J. RIEKES, LEGAL COUNSEL, THEATRE
EQUIPMENT ASSOCIATION, INC.

As legal counsel to the Theatre Equipment Association, Inc., I had the privilege of testifying before this Subcommittee on November 15, 1983, in behalf of H.R. 1157. Since the hearing on this matter was bifurcated, the second part being held on March 7, 1984, I was allowed to be present and was informed that I would be given an opportunity to respond to the latter testimony.

At the outset, several important propositions should be kept in mind:

1. Everyone has acknowledged that there is a serious problem with the present opinion molder policy because it discriminates against so many small businesses. Admittedly, there is concern from some quarters that there is a possibility that some undesirable businesses in the media industry might apply for SBA assistance. Is this concern legitimate? If it is, then is there an alternative to the present policy which does not exclude large segments of American commerce? In other words, does the baby really have to be thrown out with the bath water?

2. While we believe that the intent of H.R. 1157 is correct, we think that the language now pending before the Senate in S. 2084 offers a constructive solution to this problem, and suggest that H.R. 1157 be amended accordingly. Of course, we would also welcome any other suggested solution. We believe that Congress must take some action to resolve the problem now. The problem was presented to Congress in 1980, and the SBA promised to resolve it by regulatory reform. It did not do so, and has now placed the

matter back in the lap of Congress. There is no reason why numerous small businesses, their employees, customers, and suppliers, should continue to suffer because of the inertia of the SBA. It is a reasonable expectation of citizens adversely affected that intelligent decision makers can constructively resolve this problem.

TESTIMONY BY THE SBA

The Small Business Administration was represented by its administrator, James C. Sanders. His statement pointed in no particular direction. The essence of it was that "...[W]e welcome congressional guidance..." in this matter.

It is interesting to note that in 1980, before the Senate, the SBA insisted that it be given a chance for regulatory reform. The Administrator testified that in 1980, following the Senate hearing, the SBA published an Advance Notice of Proposed Rule making in order to alter the opinion molder policy and "to increase SBA's ability to assist small media concerns". But then the Administrator testified "SBA received a plethora of comments on the proposed changes, however, none of the proposed changes were made final." Indeed, the other SBA officials testified that they "buried" the matter. But, in correspondence in 1982, some of which is attached to our testimony of November 15, 1983, it can be seen that the SBA acted as if the events in 1980 had never occurred. If the agency had misjudged its ability to accomplish regulatory reform on its own, then it should have gone back to Congress and asked for Congressional guidance long ago. Having previously acknowledged that many small businesses were being unnecessarily disadvantaged by the opinion molder rule, it was not right to continue to leave them standing out in the cold.

During the questioning period, the SBA was unable to adequately respond to several key points. First, the SBA was not able to explain how it is that the Federal Communications Commission can deal with opinion molders, whereas it cannot. Further, in regard to motion picture theatres, in previous testimony it was pointed out that the SBA's general counsel, in 1980, specifically ruled that motion picture theatres were eligible for SBA assistance. See 117 O.D. 102. The SBA has not stated when it officially overruled this previous opinion, if indeed it ever has.

In any event, the SBA has now come before Congress and taken the position that it wishes "Congressional guidance". Given the SBA's inability to deal with these issues, then we concur and request that Congressional guidance be given, and that opinion

molders, and in particular, motion picture theatres, be extended fair and sensible treatment.

TESTIMONY OF DAVIS LEE KENNEDY

Davis Lee Kennedy, publisher and editor of the Gaithersburg Gazette, speaking only for himself, opposed H.R. 1157. He did so only on the basis that he did not think it proper, in order to maintain a rather pristine view of freedom of the press, that government in any way be connected with newspapers.

Mr. Kennedy's entire statement consisted of nothing more than mere speculation, and was without any facts whatsoever. For example, he worried that a small newspaper that received a loan from the SBA might subsequently be influenced by governmental pressure. However, he presents no evidence whatsoever that this is likely to occur. Indeed, he failed to acknowledge any difference between the electronic news media and print news media. On the contrary, it can be shown that the Federal Communications Commission, while having the ultimate power of life or death over the electronic news media, nevertheless, has not diminished the exercise of free speech by this industry. Why should it be presumed that the SBA, which has far less power over those it financially assists than the FCC, would act any differently?

Next, Mr. Kennedy tried to speculate on why the newspaper industry was not present supporting H.R. 1157. Well, they are not on record opposing it, either, and it would be endless and foolish to continue to speculate why that industry has not recorded its views. Mr. Kennedy tries to state that small newspapers do not need governmental assistance. But the answer to that, then, is that they will not apply for any loans. Further, Mr. Kennedy admits "When it comes to the theatre industry, and the effects of this rule on it, I must confess total ignorance." Why should these industries continue to be adversely affected, simply because the newspaper industry, in Mr. Kennedy's opinion, does not need nor should it have governmental assistance?

Mr. Kennedy's testimony only highlights the almost Alice in Wonderland atmosphere in which this issue has been discussed. The SBA has sat around a food barrel, for years, worrying about whether there might be a rotten apple or two inside. In the meantime, the entire media industry has been allowed to stand out in hunger. Such a situation is absurd.

Mere speculation can not be balanced with the hard reality that many small businessmen, their employees, customers and suppliers are in need of assistance. The kind of thinking re-

presented by Mr. Kennedy's testimony leads to government paralysis and not to constructive action.

STATEMENT OF ROBERT E. PARK

The final testimony of the morning was given by Professor Robert E. Park, a professor at law at the George Washington University.

While at first glance, the Professor's testimony may seem quite impressive, particularly to the layman, a closer analysis will show that the Professor spent most of his time answering the wrong questions.

For example, the Professor spent a good portion of his time in an attempt to legally justify the present opinion molder policy. While there are serious legal questions about the present opinion molder policy, that is not the real issue before Congress. If that were the primary issue, then a much more appropriate forum would be a court of law and not this Committee.

The real issue before Congress is how the SBA can fulfill its mandate in serving the widest number of small businesses, including small businesses in the media industry, without also offending any other relevant considerations.

Professor Park barely touches that subject in his written statement. In his oral testimony, he suggested that it is possible to devise regulations based upon a theme or advocacy of a particular idea approach. We would have no quarrel with Professor Park if the Committee or the SBA asked him to develop this idea further; provided, that the present opinion molder policy would be significantly narrowed so as to permit the majority of honest and decent small businesses to benefit from SBA assistance. The point is, however, that a constructive rather than an obfuscating approach is what is needed. In our opinion, the language of the Senate bill, S. 2084, will accomplish this better than Professor Park's approach.

Professor Park spends time discussing whether the small businesses excluded by the present opinion molder policy have been legally damaged. Once again, that is not the issue. Whether or not they have been legally damaged would be an issue before a court of law. The issue before Congress, however, is the fact that they have been economically disadvantaged. The testimony presented on November 15, 1983, shows that many small businessmen covered

by the present policy need help. Even the SBA admitted this when it told the Senate in 1980

"...SBA has come to the conclusion that such assistance as is required under exceptions to the 'opinion molder' rule... may not be sufficient to assist a segment of the business community which is so demonstrably in need of increased assistance."

Professor Park does not deal with this concern. But this is an issue which is the real heart of the matter. People's jobs are at stake. Since the Professor completely ignores this fundamental consideration, one wonders what his purpose in testifying was supposed to be.

The Professor should have known that no one, including Congressman Addabbo, is wedded to the precise language in H.R. 1157. Indeed, in our prior testimony we suggested amendments to H.R. 1157, which are substantially similar to S. 2084. It is Congressman Addabbo's intent, not the precise language which should be the focus. Consequently, in attacking the precise language of H.R. 1157, Professor Park has not addressed himself to the real issues. As an example, he spends a lot of time attacking the phrase "legitimate public interest" now contained in H.R. 1157. Professor Park could not be attacking that part of the phrase which are the words "public interest", since he would contradict himself if he did. He used the phrase "public interest" to give legal validity to the present opinion molder policy. Consequently, his attack is on the word "legitimate". However, the obvious solution to that problem is simply to cross out the word "legitimate" and not make so much a-to-do about it. The deletion of this word would not at all change the intent of H.R. 1157. This kind of discussion only obscures the real issues before this Committee.

There is nothing in the statute authorizing the SBA that in any way intimates that the SBA should have adopted an opinion molder policy. There is nothing in any action that Congress has taken which would intimate that it favored the opinion molder policy. Curiously, in discussing the "history" of the opinion molder policy, the Professor completely ignores the major hearing before the Senate at 96, Congress, Second Session, on S. 2873, July 24, 1980, at which time it was quite clear that both Houses of Congress, and the SBA itself, wanted the policy changed. It is inconceivable that an objective analysis could have so completely ignored this major hearing at which the present opinion molder policy was put into severe question.

Perhaps, the Professor did not see his role as providing

an objective legal analysis of the situation to the Committee, but rather as an opportunity to present his personal value judgments. For example, he admits that the present policy, while according to him is "constitutionally permitted", is nevertheless "not constitutionally compelled". He also admits that "Alternative policies could be devised to protect the First Amendment values in issue and also permit the SBA to afford financial support to some of the 'opinion molder' firms." Since the opinion molder policy is not constitutionally compelled, and there could be alternative policies to permit the SBA to be of broader service to more small businesses, why is it that the Professor spends precious little time discussing any alternative policy?

A possible explanation for the Professor's posture is his own personal belief as to what is in the "public interest". For example, it has been suggested by the San Diego Law Review article that the primary purpose of the SBA is to be a lender and not a moralizer. What is wrong with the SBA primarily using financial criteria to make its decisions? Certainly, if it did that, it would run into few constitutional questions. Obviously, the Professor does not like that position, because he wants the SBA, in fact, to be a moralizer. For example, he states "...[I]f the SBA is required to administer a loan program to 'opinion molder' firms, it is very possible that 'the public interest' tests would collapse in the mere financial criteria." He does not want this to happen because, as he speculates, it would be possible for "adult bookstores" and the like to conceivably receive SBA assistance. The Professor does not present any evidence that adult bookstores would in fact receive such loans, he is only frightened of the possibility. He ignores the facts, including SBA's own findings that "such business [e.g., sexually explicit magazines, pornographic bookstores or theatres] are generally not in need of governmental assistance..." Volume 45, Federal Register No. 197, at page 66809. So, it is much more important to the Professor that there be no possible way for an adult theatre ever to get SBA assistance, regardless of the likelihood of that possibility, than it is to be of assistance to over 3,000 theatre owners who are small businessmen. While the Professor is indeed entitled to his own value judgments, they should be identified as such.

Not only has the Professor engaged in subjective analysis, but his reasoning is questionable. He stated, "The agency believes that Congress, implicitly in its statutorily imposed public interest criterion, does not wish to give loans to activities that many people believe are socially marginal or undesirable enterprises, such as adult bookstores, ..." (Of course, as we have said earlier, the Professor has no evidence that that is the position of Congress.) However, once you begin to follow the Professor's reasoning, it leads to ridiculous results.

For example, there is no rule now that prohibits a legalized brothel in Nevada from seeking SBA assistance. Undoubtedly, many people would be upset if this were to happen. And, one could name many other types of businesses that people might believe are "socially marginal or undesirable", which are perfectly eligible now for SBA assistance. For example, there are pornographic bakeries, drug paraphernalia shops, massage parlors, palm readers, and so forth. Because it is possible that one or more of these enterprises might now qualify for SBA assistance, should the SBA no longer assist anyone? Obviously, not. But that is the very same logic that is being used against motion picture theatres and others as justification for the opinion molder policy.

There can be no absolute guarantee of either perfection or freedom from embarrassment. It is more than conceivable that persons with unsavory reputations have and will continue to receive in some instances, SBA assistance. It is virtually impossible to guarantee that will never happen unless the SBA gives assistance to no one. The public outcry in such an instance would far exceed the outcry of assistance to some socially marginal operation, if that ever occurred. Fear of possible embarrassment simply cannot, by any logic, be the *primum mobile* of governmental policy.

Furthermore, which is the greater embarrassment? Which SBA official or Congressman would like to say to the tens of thousands of people in the motion picture industry "We are sorry we cannot help you because we are worried that, should we help you, it is possible that an adult movie theatre might also be helped, and we simply cannot live with that."? This kind of logic is the real basis for the opinion molder policy. We believe that most people would subscribe to the view that it is not in the public interest to throw the baby out with the bath water.

It is also interesting that the Professor, in discussing the first amendment, ignores the argument that the opinion molder policy is impeding first amendment values rather than enhancing them by allowing the market place to be restricted. Mr. Sanders, said

"In recent years, there have been a large number of mergers and acquisitions in the media related industries which have tended to eliminate many media oriented small businesses and promoted concentration of ownership. The SBA has been concerned with the effects of this trend."

The market place for opinion molders is becoming concentrated and is shrinking. Yet, one of the prime purposes of the first

amendment is to enhance the free market place for ideas. And, thus, as pointed out by the San Diego Law Review:

"By denying financial assistance to communication-related small businesses, the SBA deprives the market place of their contribution. This hardly seems consistent with the broad scope of the first amendment."

Also, the Professor, in many places in his opinion, cites the recent Supreme Court case of Regan v. Taxation With Representation, 76 L. Ed. 2d 129 (1983). This case is cited for the proposition that it is not a violation of the first amendment rights if the government subsidizes some speech but not all speech. In other words, it is not illegal suppression of the fundamental right to free speech if some receive certain governmental benefits but others do not. The Professor uses this case in order to justify the present opinion molder policy. However, if the Professor is correct in his interpretation of this case, its very logic could be used to fashion alternative approaches to the opinion molder policy. If Congress believes that it is desirable to exclude certain kinds of businesses from SBA assistance, then this can be done. And, if the Professor is right in his analysis of the Regan case, Supra, then the logic of this case should protect those exclusions from constitutional invalidity. For instance, if it was desirable to exclude businesses primarily engaged in the sale of sexually explicit materials, then Congress ought to say so. The Regan case, and cases such as Young v. American Mini-Theatres, 427 U.S. 50 (1976), should give constitutional comfort to this approach. Likewise, newspapers or other publications that devote a substantial part of their activities in promoting or opposing candidates for public office could likewise be excluded. We do not suggest that these exclusions should be enacted. We merely suggest that these are other examples of alternative approaches, if Congress desires them. Our chief concern, as always, is that the majority of small businesses in the media industry ought not to be excluded, whatever approach is used.

S. 2084

As we have said above, the issue before this Committee is not the precise language of H.R. 1157, but a constructive solution to the problem of allowing most small businessmen to become eligible for SBA assistance, while excluding the most undesirable categories. We believe that the language in the pending Senate bill, S. 2084 introduced by Senators Sasser, Nunn, Randolph, Levin, Zorinsky and Dixon is the best solution to this problem. In introducing this bill last November, Senator Sasser stated:

"What is readily apparent to me, ... is that the opinion molder rule flies in the face of SBA's congressional mandate to aid, counsel, assist, and protect the interest of small business concerns. It is clear to me that the opinion molder rule does not encourage and develop the actual and potential capacity of small business in the United States. Instead, the rule has just the opposite effect."

"This point is not lost on SBA officials. In 1980, SBA proposed altering the opinion molder rule. This action was deemed necessary as it was felt the opinion molder rule was unnecessarily inhibiting SBA's ability to assist small business and thereby directly promoting undesirable concentration. In short, SBA feared that the rule was prohibiting it from carrying out its statutory objectives, a fear I believe is well-grounded. ...

"Unfortunately, SBA never followed through on its intentions to revise the opinion molder rule. For whatever reasons, the proposed revisions were withdrawn and small business firms across the country continued to be denied access to various SBA financial assistance programs.

"The legislation we are introducing today picks up where SBA left off. ..." Volume 129, Congressional Record, No. 155, November 11, 1983.

S. 2084 is not substantially different than the regulatory changes proposed by the SBA itself on October 8, 1980. The SBA proposed to:

"Replace the present broad proscription against assisting 'opinion molders' with specific prohibitions against certain types of assistance to certain types of enterprises. This proposal would reverse the structure of the current extremely broad rule by making small media concerns eligible for assistance unless otherwise prohibited from receiving it. This proposal would have the effect of widening the scope of media concerns to which SBA would provide assistance." 45 Fed. Reg. No. 197.

S. 2084 does precisely that.

In addition, S. 2084 makes specific and limited prohibitions:

1. It allows the SBA to deny assistance if that assistance will be "used primarily to advance or inhibit religion." This phraseology is taken directly from numerous Supreme Court cases. It is substantially the same idea, although we believe in better language, as the SBA's proposal to prohibit assistance if more than thirty percent of an applicant's annual gross income is derived from the sale, rental, or lease of religious products, materials or services.
2. S. 2084 also prohibits assistance if the assistance will be "used primarily to threaten the overthrow of organized government by unlawful means." This phraseology is also familiar to the courts. The SBA had suggested denying assistance to enterprises which advocate a particular religious, political, social, or economic point of view, as opposed to general media concerns. This is basically Professor Park's theme idea, but such an approach might find the SBA in difficulty in determining what is particular and what is general.
3. S. 2084 would allow the SBA to deny assistance where assistance will be "used primarily to engage in any illegal activity or the dissemination of obscene materials which may be unlawful in any jurisdiction in which the small business concern may operate."

We believe that the language just quoted is similar to SBA's prior suggestion to deny assistance to an applicant if more than thirty percent of its annual gross income is derived from the sale, rental or lease of sexually explicit products. Under the teaching of Miller v. California, 413 U.S. 15, obscenity is a matter of local concern. Under S. 2084, if the SBA, in determining the credit-worthiness of an applicant, believed that there was a good probability that the applicant might run afoul of any community standard and law in which it might operate, then the SBA could lawfully deny assistance to that applicant. The SBA would be making this determination as a lender, not as a censor nor as a court.

The Senate bill provides that the SBA may not deny financial assistance in the form of guarantees to any small business concern

solely because it is an opinion molder. Thus, the bill adopts the previous SBA suggestion that a distinction be made between direct loans and loan guarantees. The SBA stated:

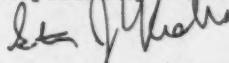
"This proposal would be a reasonable accomodation between SBA's desire to assist eligible media enterprises while minimizing the danger of actual or apparent government censorship of the media."

In our judgment, S. 2084 is sound legislation. It adopts what the SBA said it was going to do and never did. Ironically, the opinion molder policy designed by the SBA to protect it from embarrassing situations, has itself become a virtual fountain of embarrassment. S. 2084 rescues the Agency from its own debacle.

We believe that this Committee should seriously look at S. 2084 and consider amending H.R. 1157 to conform therewith, and then to approve it so that this problem can once and for all be resolved.

In support of the legal validity of S. 2084, plus some other comments about this situation, we are also pleased to attach the opinion of Professor Richard Shugrue of Creighton University Law School, a very eminent constitutional scholar.

Respectfully submitted,



STEVEN J. RIEKES

SJR/bls

APPENDIX C

STATEMENT OF RICHARD E. SHUGRUE

BEFORE THE SUBCOMMITTEE ON
EXPORT OPPORTUNITY AND SPECIAL
SMALL BUSINESS PROBLEMS

UNITED STATES HOUSE OF REPRESENTATIVES

INTRODUCTION

Mr. Chairman, I am Richard E. Shugrue, Professor of Law at Creighton University, Omaha, Nebraska. This statement is prepared in response to a request by Mr. Steven J. Riekens, Legal Counsel for the Theatre Equipment Association, Inc. My conclusions on the "Opinion Molder" rule of the Small Business Administration and on the constitutionality of proposed amendments to the Small Business Act are my own and do not represent the policy of the TEA nor of Creighton University.

I earned my A.B., J.D. and Ph.D. degrees from the University of Nebraska at Lincoln, my doctorate having been awarded in the field of public law. I have taught courses in American Government and Administrative Law and have been a professor of law since 1971. I currently teach Constitutional Law and have written and lectured extensively in the area of First Amendment Rights.

SUMMARY OF CONCLUSIONS

1. The opinion molder rule is an ill-conceived regulation which departs from the genuine charge to the Small Business Administration from the Congress of the United States. It is riddled with inconsistencies, has been swallowed up by exceptions and serves little if any legitimate interest of the public at large or of the small business men and women who should be served by the S.B.A.

2. The public is best served by a legislative amendment which would eliminate the opinion molder rule. The type of language contained in the Senate version of an amendment, S. 2084, will survive current constitutional scrutiny. The exclusions in the amendment do not amount to impermissible content regulation, nor are they vague. The Congress is free to extend the largesse of the public treasury and other forms of assistance to whatever categories it deems in the public interest. The categories contained in S. 2084 are ones which are entitled to no special treatment at the present time under the Constitution.

INTRODUCTION

The Small Business Administration is mandated by Congress to aid, counsel, assist and protect the interest of small business concerns. With the adoption of the opinion molder regulation and the illogical exceptions to that rule, the agency has unilaterally deprived large segments of the American business community, both urban and rural, from the very succor which our lawmakers have decreed to be the central mission of the S.B.A.

For whatever motives--potential embarrassment, timidity or a desire to disregard the charge dictated by elected representatives--the S.B.A. has promulgated and perpetuated the opinion molder rule, even though officials of the agency itself as well as members of Congress and victims of this

ill-conceived unilateral principle have decried its deleterious impact on the public.

Critics of the rule have uncovered as a sham the suggestion that the elimination of the regulation would create untold constitutional problems and result in a proliferation of litigation.

While the rule may be constitutionally permissible under Equal Protection and First Amendment analyses, the fact remains that its elimination by a well-considered proposal, such as S. 2084, would not only eradicate the inconsistent exercise of arbitrary power now enjoyed by the S.B.A. but also would serve better the interests of a healthy cross-section of American business people, citizens who are ill-served by the current policy.

An elimination of this rule would, moreover, carry with it the eradication of the bizarre exceptions to the rule's application. These exceptions swallow up whatever so-called "public interest" justifications have been said to exist for the rule. They make little if any sense in light of contemporary constitutional principles or, for that matter, current operations within the free-enterprise market place.

I. THE S.B.A.'S POSITION

Administrator James C. Sanders of the S.B.A. has advanced three reasons for the maintenance of the opinion molder policy. First, to avoid Government interference or the appearance of such interference with the constitutionally protected freedoms

of speech or press by subsidizing the publication of ideas which promote particular political views or propaganda. Second, to avoid the possibility of creating an unconstitutional prior restraint on the expression of ideas by applicants. Third, to avoid lending to concerns which publish or produce or sell materials of a highly controversial nature, which, while not illegal, may not be in the public's interest to promote. (Statement before the Committee on Small Business, Subcommittee on Export Opportunities and Special Small Business Problems, House of Representatives, March 7, 1984.)

At the same time the agency has advanced these reasons, the S.B.A. has promulgated seven regulatory exceptions which include: commercial or job printing firms; publishers of shoppers' newspapers or circulars composed completely of advertising materials; firms producing advertising and technical materials; broadcasting and cable television operators; vocational, technical, and other nonacademic schools and general book or music (record) stores, and general merchandise stores which may sell books, newspapers, magazines, records, etc.

It is submitted that the very existence of these exceptions has swallowed up the rationale for the opinion molder rule and comports neither with common sense nor with the true objective of the S.B.A., as dictated by Congress: the assistance of small business in this nation.

Moreover, Small Business Investment Corporations may be created which provide forms of assistance to any business, irrespective of its nature. Thus, there is built into the

administrative structure of aid programs a generic exception to the opinion molder rule. This generic exception, by definition, makes even less sense than the specific exceptions, if consistency is the goal.

Examine these exceptions for a moment.

A commercial printing firm is in the very business of serving as a conduit for ideas. It may have contracts with pro-lifers to publish their tracts, with the gay rights movement to public broadsides, with fundamentalists to print their magazines. It is entitled to aid, unless, of course, the S.B.A. stands over its shoulder and determines, publication by publication, the form of product which would make it inelligible to obtain support. The printer is as surely an opinion molder as Benjamin Franklin's printing shop was. In the case that a determination is made that certain products may not flow from the presses, the very "anti-censorship" rationale of the S.B.A. dissolves.

Publishers of shoppers' newspapers. These are often wholly owned subsidiaries of general circulation publications. The income from the shopper enables the general circulation press to espouse its ideas, even expand its coverage, because of the classified paper's income. The "gold-mine" may be funded; the beneficiary may not.

Firms producing advertisements and technical materials. The awesome power of the advertising industry was once again illustrated for the public by Newsweek, March 26, 1984, pp. 62-64. The reader is told, "The growing acceptance of sex as a selling tool has also led to some remarkable innovations."

The article goes on to report that "bare breasts are peeking out at readers from Calvin Klein underwear ads . . . and even the ultracautions networks are allowing some obviously erotic commercials on the air." "The networks gave their stamp of approval to a new Chanel No. 5 commercial, despite the ad's obviously phallic closing shot."

If the S.B.A.'s justification for the opinion molder rule is to "avoid lending to concerns which publish or produce or sell materials of a highly controversial nature, which, while not illegal, may not be in the public's interest to promote," how could any stretch of the imagination justify this exception?

Broadcast and cable television operators are excluded from the opinion molder rule's inelligible list. Notwithstanding any sanctimonious pretense that cases such as F.C.C. v. Pacifica Foundation, 438 U.S. 726 (1978) provide a regulatory blanket for commercial broadcasters, the fact remains that one need only flip his or her dial to the cable "premium" channels to see material which is at least "of a highly controversial nature." Its purveyors, nevertheless, are eligible for S.B.A. help.

Vocational, technical and other nonacademic schools. This, presumably, means automotive repair institutes and their ilk. But, even if it does, one may ask whether the S.B.A. routinely examines the curriculum and presentation to be certain that no "ideas" are taught? Including ethics in the market place? Including the ability of a tradesperson to communicate in literate English?

General book or music (record) stores. It is inconceivable that the S.B.A. could advance its justifications for the opinion molder rule and at the same time defend this exception. Any general book store worth its salt will stock hundreds of controversial publications. Unless the S.B.A. is staffed with psychoanalysts it simply cannot know what motivated the book seller to order five copies of this and ten of that. As a result the agency places itself in the impossible position of denying assistance because, for example, of the trade name of the shop. Thus, "Kieser's Book Store" is helped and the "Gay Outlet" is denied. To paraphrase Justice Holmes in Gitlow v. New York, 268 U.S. 652 (1925), every book contains opinions.

Equally interesting is how and why the agency determined to include general book stores for assistance but eliminated eligibility of general movie theatres. If it is argued that general book stores only select titles which will sell (a commercial decision), then how can the S B.A. reach the conclusion that general theatres make their decisions on any other form of determination? This is particularly true in a day and age of multi-screen general theatres in which it is obvious that the selection of shows has every bit as much to do with "hit" status as selection of books in a store has to do with "best seller" status.

The unvarnished truth of the matter is that a catholicity of ideas is the very foundation of a free society. To deny purveyors of ideas the right to participate in a government program is the antithesis of democratic "public interest."

But, of course, the S.B.A. recognizes (grudgingly) what any reasonable person knows by looking at the opinion molder rule, its justifications and its exceptions. It is a rabbit's warren of inconsistency, self-proclaimed "public interest" and illogical results.

The Statements of Steven J. Riekes before the House Subcommittee and the Senate Committee have accurately and precisely chronicled the posturing of the S.B.A. regarding the opinion molder rule. An examination of those statements and of the supporting citations reveals that the agency acknowledged a strong sentiment in both Houses of Congress for a change in the policy. The agency recognized that the policy had produced inconsistent results. It proposed several alternatives (45 Federal Register 197, October 8, 1980) and then, apparently, abandoned its good intentions.

The Congress of the United States now has the opportunity to get rid of the opinion molder rule. To this end, H.R. 1157 and S. 2084 have been introduced.

H.R. 1157 is the less desirable for it is the less precise. It would deny assistance if it would be (A) adverse or detrimental to a legitimate public interest, or (B) used primarily to promote or criticize political or religious ideas. It was just such focus on illusory notions of "public interest" which precipitated the S.B.A.'s adoption of the opinion molder rule in the first place. The agency substituted its own judgment as to what was in the public interest for that of the broad mission statement contained in the original act.

The language found in (2)(A) is too great a temptation to substitute bureaucratic determinations of what is in the public interest for the legitimate findings of the Congress.

Moreover, the language in (2)(A) provides no guidance to the agency as to the meaning of the words "promote", "criticize", "political" or religious". Past experience teaches the painful lesson that an overzealous or intimidated agency might draw its own conclusions on these words, thus foreclosing thousands of small businesses from the opportunity to participate in an important government program.

The Senate bill, S. 2084, on the other hand, contains categories about which solid determinations have already been made. The government may not now advance nor inhibit religion, Lemon v. Kurtzman, 403 U.S. 602 (1971). It now treats obscenity differently from those classes of expression protected under the First Amendment; Miller v. California, 413 U.S. 15 (1973). Moreover, the government may now punish utterances endangering the foundations of organized government and threatening its overthrow by unlawful means. Gitlow v. New York, 268 U.S. 652 (1925).

II. AN ANALYSIS OF THE CRITIQUES OF CHANGE

A. Professor Park

The current opinion molder rule is defended by Professor Park on several grounds.

He argues that the rule is constitutional, that it is permitted but not compelled. He maintains that it is consistent with the public interest mandate of the S.B.A. It is respectfully submitted that nothing could be further from the truth. The mandate of the agency is to assist small businesses. It has assumed unto itself the right to draw broad, inconsistent lines between the types of businesses it deigns to help and those it leaves out. It does so with no citation of relevant authority and it does so notwithstanding the fact that it recognized in 1980 the inconsistent results flowing from the rule.

Professor Park argues that an elimination of the opinion molder rule may complicate loan administration. It is submitted that it is the very present policy which, indeed, complicates the administration of loans. For this policy is wedded to the notion that the agency can differentiate between those businesses it has unilaterally excluded and those it includes in its list of seven exceptions. That the agency has not been inundated by a rash of litigation over its caprice is both amazing and a tribute to the patience of the American business operator.

Having conceded that the opinion molder rule and its exceptions can survive application of Regan v. Taxpayers With Representation, 76 L.Ed.2d 129 (1983) one surely must

concede that the Senate version, with its narrowly drawn, consistent exceptions could survive such minimum-rationality scrutiny as well.

But the reader of Professor Park's statement is told that the agency does not wish to be associated with controversies; that it does not want to be seen as endorsing racism, smut or adult films. In truth, the agency is up to its withers in controversy because of its own inconsistency.

The Senate version of the bill would allow the S.B.A. to exclude those very categories which it may consciously or not be including now.

But even if that were not the case, government assistance programs ought not be designed or administered with the end of administrative convenience in mind.

Professor Park posits the idea that the present public interest tests might collapse into mere financial criteria. As a matter of fact, that is the way the government is supposed to operate a program such as small business assistance. Let the Congress set the public policy. Let the agency administer it, rather than shape it to its own convenient notions.

In fact, Professor Park's very "public interest" justification for the current opinion molder rule is turned on its head in his criticism of the House version of the bill, where he argues in paragraph 204 that H.R. 1157 has no definition of legitimate public interest. Any fair reading of the present legislation and the rules promulgated pursuant thereto demonstrates that the S.B.A.'s idea of public interest

is fabricated out of whole cloth and, in truth, the rules clearly ignore the only legitimate (and clear) statement by the Congress itself.

Finally, Professor Park suggests that the opinion molder rule is substantially less threatening to First Amendment values and rights than is frequently suggested by those who dislike the rule. He is concerned (as are others) that the amendments, H.R. 1157 and S. 2084, rather than being legitimate categories, and thus can survive constitutional review, are content-oriented prior restraints. This is, indeed, a curious position for one to take who has acknowledged that the opinion molder rule has some classes which are clearly not content neutral (Park Statement, Paragraph 203).

What he and the other critics of legislative reform simply ignore or have failed to see is that the Supreme Court of the United States currently is not bothered by such distinctions. The government has no obligation to fund the exercise of fundamental constitutional rights. It quite obviously has no obligation to fund activities which are not protected by the constitution, such as promulgation of obscenity, the advancement of religion or armed revolt.

As will be demonstrated, the cornerstone of the funding-constitutional rights controversy's resolution is the premise that there is a basic difference between direct state interference with a protected activity and state encouragement of an alternate policy consonant with legislative goals. Maier v. Roe, 432 U.S. 464, 475 (1975). (See, Perry, The Abortion

Funding Cases: A Comment on the Supreme Court's Role in American Government," 66 Geo. L. J. 1191 (1978)).

That case made it clear that a penalty, and thus a right to complain, exists only if the government withdraws more than the monetary cost of exercising the disfavored alternatives. 432 U.S. at 474-75. See, "Supreme Court Upholds Validity of Hyde Amendment," 14 Creighton L. Rev. 607, 621-623 (1981).

The concern about content regulation in a grantsmanship context may be a function of the fact that, over the years, there was little guidance as to how these conflicts would be resolved. Cappalli, "Federal Grant Disputes: The Lawyer's Next Domain," 11 Urban Lawyer 377 (1979). Some people now may fail to differentiate between the exercise of a right and the necessity to extend a privilege to all comers.

Professor Park is correct in stating that the opinion molder rule is constitutionally permissible. That rule concededly contains some element of content approval. But as Judge Campbell stated in another context in Advocates for the Arts v. Thomson, 532 F.2d 792, 795-796 (1st Cir. 1976), to focus on it is beside the point. The government may make a rationally based policy to fund whom it will, and to exclude whom it will. Neither the First nor the Fifth Amendment gets in the way of this policy choice.

B. The Justice Department Statement

In his letter to Senator Lowell Weicker, Jr., concerning S. 2084, Assistant Attorney General Robert A. McConnell argues

that the standards for denying financial assistance under the bill are very broad and vague, and they thus may prove difficult to administer.

He secondly argues that the breadth and vagueness of the definitions fail to comport with the strict standards required when limits are placed on First Amendment activities.

As indicated elsewhere in this memorandum, even if a potential recipient of government financial assistance had a property right in such aid (which is not the case), and even if strict scrutiny were the standard of review in an appropriate suit, the exclusions in S. 2084 would surely pass constitutional muster.

1. On the aid to or inhibition of religion, the guiding doctrine was established in Walz v. Tax Commissioner, 397 U.S. 664 (1970) where the Court tested a tax exemption for religious entities. Chief Justice Burger wrote that any aid program would be invalid unless it (1) had a secular purpose; (2) had no primary effect of advancing or inhibiting religion; and (3) avoided being an "excessive entanglement" between government and religion. (emphasis added) 397 U.S. at 664.

Again in Lemon v. Kurtzman, 403 U.S. 602 (1971), the Court reiterated its "primary effect" test. In Committee for Public Education v. Nyquist, 413 U.S. 756 (1973), the primary effect rubric was utilized to nullify a parochial school assistance program. See also Sloan v. Lemon, 413 U.S. 825 (1973).

Even more recently, in Committee for Public Education and Religious Liberty v. Regan, 444 U.S. 646 (1980), the Court

continued to look to its three-part test, including, of course, the "primary effect" element, as the definitive body of law on aid to religion.

Time after time, the Court's own words, "primary effect" have been used with precision to test aid-to-religion cases. To suggest now that it is unconstitutionally vague is to deny the persistent rule adhered to by the Court.

2. The second definition would deny aid to those businesses when the assistance would be used primarily to threaten overthrow of organized government by unlawful means. This definition is a virtual tracking of the provisions of 18 U.S.C. 2385, held constitutional in Dennis v. United States, 341 U.S. 494 (1951).

3. The final category focuses on dissemination of obscene materials made unlawful in any jurisdiction of the land. One of the elements of the landmark Miller v. California, 413 U.S. 15 (1973) test for obscenity was whether the work depicts or describes, in a patently offensive way, sexual conduct specifically defined by the applicable state law. 413 U.S. at 24.

The Court explicitly acknowledged that under Miller the state courts are allowed to save their statutes, even when they do not list the categories of offensive materials, by construction and in so doing expand the Court's list of examples. 413 U.S. at 27.

Any national standard for obscenity, as suggested by the no-majority opinion in Jacobellis v. Ohio, 378 U.S. 184 (1964) was specifically rejected to Miller. 413 U.S. at 26.

If any of these definitions is constitutionally vague, it must be because of some decision of the courts unknown to this writer. It seems, rather, that they have been carefully drawn to comport with contemporary precedent and would be sustained if challenged.

The Justice Department cites Hynes v. Mayor of Oradell, 425 U.S. 610 (1976) and Big Mama Rag, Inc. v. United States, 631 F.2d 1030 (D.C. Cir. 1980).

Hynes dealt with a canvassing ordinance which required advanced notice to the city "for identification only" by a person soliciting for a "recognized charity." The ordinance was struck down as vague: it did not explain the meaning of "recognized" charity nor of adequate "identification." Chief Justice Burger indicated that these ambiguities gave police the effective power to deny permission to canvass for political causes.

This case involved a proscription of the conduct and not the issue of whether the government must pay for it.

In Big Mama Rag, the controversy surrounded the denial of tax exempt status to an organization which could not demonstrate to the satisfaction of the I.R.S. that it was "educational" and would give full and fair exposition to all points of view.

If the Justice Department were truly concerned with vagueness in the case of the S.B.A., it would seem far more appropriate that this case be cited for the proposition that the current exceptions coupled with the opinion molder regulation allow aid to "non-academic" schools or "general" book stores.

The Court in Big Mama Rag cites Speiser v. Randall, 357 U.S. 513 (1958), for the proposition that although First Amendment activities need not be subsidized by the state, the discriminatory denial of tax exemptions can impermissibly infringe free speech. 631 F.2d at 1034.

The material distinction, however, is drawn in Regan v. Taxpayers With Representation.

III. A CONSTITUTIONAL ANALYSIS OF S. 2084

S. 2084 would deny financial assistance to any small business concern if a determination is made that such assistance will be--

- (A) used primarily to advance or inhibit religion;
- (B) used primarily to threaten the overthrow of organized government by unlawful means; or
- (C) used primarily to engage in any illegal activity or the dissemination of obscene materials which may be unlawful in any jurisdiction in which the small business concern may operate.

The constitutional issues which may be involved with such exceptions are really no different from the constitutional problems inhering in the present opinion molder rule. If the government is constitutionally prevented from denying aid to any colorably protected activity, then it is prevented from denying aid to some colorably protected activity. Having

conceded that the present rule allows a "few narrow and special classes" of opinion molders to receive aid, Professor Park proceeds to say that the opinion molder rule violates neither the applicable First Amendment or Equal Protection doctrine. The agency does have to decide, under its own, present rule, whether a bookstore is general or special. In making that determination, if it currently violates no constitutional norm, then in making the decisions under S. 2084, it could not be breaching the rules.

But more importantly, one must begin an analysis of any funding scheme legislation or rule with the question, "May the rule makers exclude any arguably protected activity from being eligible for assistance?" If the answer is that all such an exclusion must be measured against is a merely rational determination of what activities will be funded, that ends the inquiry.

It certainly ends the inquiry where Congress has chosen for exclusion from a program activities which are either traditionally not protected or which have traditionally been ineligible for any government assistance.

In the former class, for example, falls obscenity. Whatever protection speech and the press are entitled to under the First Amendment, obscenity is excluded from that treatment and has been from the time of Roth v. United States, 354 U.S. 476 (1957) through Miller v. California to the present day. As to those traditionally not aided by the government, any list would

be headed by religious activities which at once are insulated from interference by the Free Exercise clause and prevented from being governmentalized by the Establishment clause. See, e.g., Walz v. Tax Commissioner.

But in the area of government largesse, even if a constitutionally protected right is at stake, the Supreme Court has never held that Congress must grant a benefit to a person who wishes to exercise the right. Regan v. Taxpayers With Representation, 76 L.Ed. 129, 137 (1983). The Court specifically rejected the holding of the Court of Appeals that strict scrutiny should apply whenever Congress subsidizes some speech but not all speech. Id., at 138.

Had there ever been any doubt that Congress must merely have some rational basis for drawing lines between those eligible for assistance and those excluded, the question was laid to rest once and for all in the so-called abortion funding cases.

These, the Court was dealing not problematically with some alleged constitutional right, but with the privacy-freedom-of-choice guarantees which it found to exist in Roe v. Wade, 410 U.S. 113 (1973). Thus, the resolution of whether a person seeking an abortion is entitled to government aid clearly and sharply resolves the question of whether someone advancing a questionable constitutional right, such as purveying obscenity or attempting to have his or her church funded, may be excluded from the program.

In a series of modern cases, the majority of the Court consistently has held that the state need not subsidize the financing of the constitutional right for those who lack the economic resources to obtain it. Maher v. Roe, 432 U.S. 464 U.S. 438 (1977), Harris v. McRae, 448 U.S. 297 (1980) and Williams v. Zbaraz, 448 U.S. 358 (1980).

This distinction is based upon the Court's view that the right to privacy regarding abortions involves only the absence of express governmental limitations on the abortion decision. The failure to subsidize these practices constitutes no more than a policy choice not to give increased wealth or welfare benefits to a class of people who are not described by any suspect trait. Nowak, Rotunda and Young, Constitutional Law (2d ed. 1983, p. 731).

Compare this analysis with that in Regan v. Taxpayers With Representation, where the Court stated that Congressional selection of particular entities or persons for entitlement is "obviously a matter of policy and discretion not open to judicial review" unless in circumstances not present in Regan, and certainly not present in a fair analysis of S. 2084. 76 L.Ed. at 139.

The significance of the abortion funding cases cannot be overemphasized in any contemporary attempt to analyze the treatment of all government assistance programs.

This line of cases merely fleshes out the sketchy analysis available before the late 1970s and early 1980s. Cammarano v. United States, 358 U.S. 498 (1959), denying business expense deductions for lobbying activities, was merely a wisp of a clue as to how the modern Court could treat competing demands upon the public fisc. Most recently, cases such as Bob Jones University and Regan v. Taxpayers With Representation put to rest any doubt that the Congress was free to make policy choices as to who should benefit from special tax treatment.

The abortion cases are the collective capstone placed on the public funding debate. The process of sorting out the distinction between interfering with the exercise of a right and the choice not to fund that exercise began in the last decade, perhaps, with Johnson v. Robinson, 415 U.S. 361 (1974) where the Court noted that the failure to provide veterans benefits to conscientious objectors presented absolutely no First Amendment problems.

That decision is coupled with Buckley v. Valdo, 424 U.S. 1 (1976), where the Court ruled that a legislature's decision not to subsidize the exercise of a fundamental right does not infringe upon the right and thus is not subject to strict scrutiny.

Jurists, scholars and lawyers have been concerned that the failure to fund in certain kinds of cases may impinge fundamental rights and thus must pass the strictest of

scrutiny. To be sure, the interference with the exercise of First Amendment rights, when the governmental conduct is active, is subject to the highest level of review.

The abortion funding cases teach that governmental protection of those without resources is a matter to be resolved democratically in accordance with majoritarian will. Harris, at 448, said that in a democracy, policy choices are to be resolved by the legislature. Maher and Roe hold that when a state simply fails to subsidize the exercise of a right, the rationality standard controls.

McRae's doctrine is that if state action deprives an individual of something that otherwise belongs to him, he has been penalized. But this type of deprivation (forbidding an adult bookstore from opening, banning a preacher from the park, denying a license to a political group for a rally) is analytically distinguished from mere refusals to subsidize protected activity. See Appleton, "Beyond the Limits of Reproductive Choice: The Contributions of the Abortion-Funding Cases to Fundamental-Rights Analysis and to the Welfare-Rights Thesis", 81 Columbia L. Rev. 721, 733 (1981).

Thus, just as the question of whether the constitutionally protected freedom of choice warrants federal subsidization is a problem for Congress to answer, and not a matter of constitutional right, the issue of whether an adult bookstore (or any bookstore) is entitled to government largesse is a policy choice for the lawmakers to resolve.

Now, if that be true where the protected activity is constitutionally guaranteed, it is clearly true where the activity is not guaranteed. The First Amendment protects neither obscenity as appropriately defined by state law nor the "right" to have the state build a church. Funding choices relating to such subjects, then, are far beyond any hint of a constitutional cash entitlement.

To confuse the funding cases with content censorship decisions such as Grayned v. Rockford, 408 U.S. 104 (1972), or Chicago Police Dept. v. Mosley, 408 U.S. 92 (1972), is to confuse the notion of active government conduct with the kind of passive inaction which is the predicate of all the modern funding litigation.

To be sure, cases such as Mosley and Grayned and, more recently, Carey v. Brown, 447 U.S. 455 (1980), have continued to advance the rule that the state may not interfere with legitimate, protected activity based on the content of that activity. Carey, for example, struck down a ban on residential picketing which gave a preference to labor picketing over other forms of protected speech.

None of these cases mandated that the government pay for the picket signs. Nor did they say that even if the government somehow subsidized some forms of expression, it had a duty to subsidize all forms of expression, legal or not.

While the rule is clear that the government may not elect between forms of expression it tolerates, it is equally clear that it is free to choose what activities it wishes to subsidize.

Anyone who takes the time to scour the legal literature may be stunned to discover that despite the myriad of government programs which provide any form of assistance to citizens, the abortion cases are the only ones which persistently and directly relate to the constitutional questions arising from a rights-entitlement debate. They are comprehensive resolutions of the types of questions cautious men and women faced with drafting legislation such as S. 2084 or H.R. 1157 must surely raise. Coupled with the tax cases, such as Regan v. Taxpayers With Representation, they serve as steady guideposts for resolving any ambiguities which may arise.

Two cases dealing with demands upon the fisc are instructive. In the first, Advocates for the Arts v. Thomson, 532 F.2d 792 (1st Cir.), cert. denied, 429 U.S. 894 (1976), state officials, grantees of federal funds, determined not to grant aid to a literary magazine because the latter had published "obscenities" in the past. In the majority opinion, Judge Campbell considered the question of whether a decision not to fund a particular arts project based on nothing more than personal preferences constitutes a prior restraint of free expression.

Judge Campbell wrote:

A disappointed grant application cannot complain that his work has been suppressed, but only that another's has been promoted in its stead. . .

(The magazine's) claim of arbitrary treatment . . . is essentially a claim of denial of due process. Yet in the absence of any right to public support of private expression, it seems unlikely that (the magazine) has a sufficient "liberty" or "property" interest in a favorable decision to be able to claim a right to procedural regularity under the fourteenth amendment. 532 F.2d at 795-798.

Citing Jaffe, "The Illusion of the Ideal Administration", 86 Harv. L. Rev. 1183 (1973), Judge Campbell repeated the axiom that it is ultimately the prerogative of elected officials to decide when and how to spend the tax dollar, and those administering grant programs cannot ignore the importance of continued legislative and executive confidence in their judgment.

The second case, Legal Services Corporation v. Ehrlich, 457 F. Supp. 1058 (D. Md. 1978) involved a complaint that the federal legal services corporation denied it grants to permit it to render services. (The case was not a challenge to federal legislation which forbids legal aid attorneys from engaging in political activities (42 U.S.C. Section 2996e(3)).

But the case held that procedural rights under the Fifth Amendment exist only if plaintiffs have liberty or property rights with respect to obtaining grants. The Court held that

in the absence of congressional creation of such rights, they have none. 457 F. Supp. at 1064.

CONCLUSION

What is clear from the funding cases discussed is that the Supreme Court has developed, over the last several years, a rule which vests in the lawmaking body the sole discretion to determine who shall obtain grants and other forms of government assistance. This democratic, majoritarian process to which the greatest of deference is given is neither a prior restraint nor a form of rights impingement.

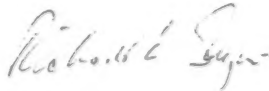
Persistent constitutional principles, based on the fundamental law itself, as definitively interpreted by the Court, provide more than ample bases for excluding certain forms of activities from participation in loan or loan guarantee programs.

S. 2084 is a model of clarity. It captures the essence of the original broad public charge to the SBA in that it includes as eligible for assistance a wide range of legitimate American businesses now arbitrarily excluded. It carves out as exceptions those categories which suffer no infirmity or vagueness.

In providing for review, it creates a mechanism for resolving any question as to lack of due process guarantees.

But most importantly, it eliminates the caprice of the unilaterally written policy of the agency which currently has the effect of crippling the aspirations of thousands of enterprises which seek legitimate cooperation from their government. S. 2084 can survive any assault on constitutional grounds. It has the distinct advantage of reestablishing the exclusive right of Congress to set national policy and oversee the important work of the agency. In assessing the problems in H.R. 1157, the House is well-advised to look to the wording of S. 2084 for guidance.

Thank you.



Richard E. Shugrue

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